

# Modern Real Estate Practice Workbook

Fifth Edition

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MODERN REAL ESTATE PRACTICE WORKBOOK FIFTH EDITION

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# UNIT 1

## Introduction to the Real Estate Business

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › List the various careers available in the real estate industry.
- › Describe the different classifications and characteristics of real property and the types of housing available for purchase or rental.
- › Explain the factors of supply and demand in the real estate market.

### KEY POINTS—UNIT 1

- Real estate brokerage is the business of bringing people together in a real estate transaction.
- A real estate broker is a person or company licensed to buy, sell, exchange, or lease real property on behalf of others for compensation.
- A real estate salesperson is employed by or associated with the broker to perform brokerage activities on behalf of or for the broker, and may also be referred to as a sales associate or an associate licensee.
- A real estate licensee is someone who has satisfied the requirements of a licensing agency, as authorized by state legislation.
- An appraisal is the process of developing an opinion of value.
- Appraisal licensing or certification is required for federally related transactions.
- Property management services are provided by a property manager who may be required to be a licensed real estate brokerage or licensed property manager to maintain and manage property on behalf of the property owner. The property manager's scope of work depends on a management agreement, and the basic responsibility of the property manager is to protect the owner's investment while maximizing the owner's financial return.
- Financing is the business of providing the funds that make real estate transactions possible through loans secured by a mortgage or deed of trust on the property, with funding provided by commercial banks or credit unions, as well as mortgage bankers and mortgage brokerage companies.

- Federal law requires mortgage loan originators to qualify for the Nationwide Multistate Licensing System and Registry (NMLS).
- Subdivision and development involve splitting a single property into smaller parcels (subdividing) and constructing improvements on the land (development).
- Home inspection, used by both purchasers and homeowners, provides an inspection report that shows the results of a thorough survey of observable property conditions. Many states require home inspectors to be licensed.
- Real estate counseling involves independent advice based on sound professional judgment regarding how to buy, sell, or invest in property.
- Real estate education is provided by a variety of sources to practitioners and consumers.
- Types of real property include residential, commercial, mixed-use, industrial, agricultural, and special purpose, which can be privately or publicly held.
- Housing in the United States includes the single-family detached house, the multi-unit structure that often is owner-occupied, the apartment building, the condominium or cooperative, the planned unit development (PUD), the converted-use building, and factory-built structures.
- The real estate market reflects the principle of supply and demand, influenced by the uniqueness and immobility of parcels of real estate. When the supply increases relative to demand, prices go down, and when demand increases relative to supply, prices go up.
- The factors affecting the supply of real estate include labor force availability, construction and material costs, government controls (environmental restrictions, land-use policies, building codes, zoning), and monetary policy that impacts interest rates and the money supply.
- The factors affecting the demand for real estate include population, demographics, employment, and wage levels.
- A homebuyer can benefit from tax deductions, exclusion of gain on the sale of the home, and tax credits, when available.
- The federal income tax code offers homeowners numerous tax benefits, including the deduction of mortgage interest, property taxes, and points, and the exclusion of a gain of up to \$250,000 (single) or \$500,000 (married) on the sale of a principal residence owned for at least two of the previous five years.

## I. REAL ESTATE SPECIALIZATIONS

### A. Brokerage

1. The business of bringing people together in a real estate transaction
2. Brokerage activities: help others buy, sell, or lease real property
3. A broker/brokerage/firm is
  - a. a person or company,
  - b. licensed to perform brokerage services for a client for a fee, and
  - c. may employ other real estate licensees.

4. A salesperson/sales associate/broker associate
  - a. is a person employed by or associated with a broker,
  - b. performs brokerage services for the broker, and
  - c. may not provide brokerage services independently.
5. Clients hire the brokerage firm.
6. Terms such as *real estate agents*, *licensees*, and *professionals* include all firms, brokers, and salespersons.
7. Real estate agents must be licensed in each state where they practice, unless the state has a reciprocal licensing arrangement with another state.

## **B. Appraisal**

1. The process of developing an opinion of a property's market value, based on established methods and the appraiser's professional judgment
2. Appraisers must be licensed by the state.

## **C. Property management**

1. A property manager is a person or company hired to maintain and manage property on behalf of the property owner.
2. Depending on the state, a property manager must be a licensed real estate broker or property manager.

## **D. Financing**

1. The business of providing funds for real estate sales transactions
2. Mortgage loan originators (MLOs)
  - a. Registered with the Nationwide Multistate Licensing System (NMLS)
  - b. Licensed by the state

## **E. Subdivision and development**

1. Buy property, add value, sell, or rent
2. Subdivision: dividing a single property into smaller parcels
3. Development: site preparation, construction of structures, and other improvements

## **F. Home inspection**

1. Combines a practitioner's interest in real estate with skills and training in the construction trades
2. Some states require licensing.

**G. Counseling**

1. Provides clients with information needed to make informed decisions
2. Helps clients choose among the various alternatives involved in purchasing, leasing, using, or investing in property

**H. Education**

1. Provided by colleges and universities, private schools, and trade organizations
2. Available to licensees and consumers
3. State licensing laws establish minimum educational requirements.
  - a. Prelicense education—to obtain a license
  - b. Continuing education—to maintain and renew a license

**I. Other areas**

1. Real estate law
2. Land-use planning
3. Real estate research
4. Tax assessment

**II. TYPES OF REAL PROPERTY****A. Six categories of real property**

1. Residential
  - a. Structures in which people live
  - b. Single-family and multifamily housing
2. Commercial
  - a. Office, retail, entertainment, hotels, parking structures
3. Mixed use
  - a. Commercial and residential uses in the same building or development
4. Industrial
  - a. Warehouse, manufacturing, land in industrial districts, power plants

5. Agricultural
  - a. Farms, timberland, ranches, and orchards
6. Special purpose
  - a. Places of worship, schools, museums, cemeteries, municipal service buildings, and parks
  - b. Privately and publicly owned

### **III. TYPES OF HOUSING**

- A. Single-family detached**
- B. Apartment building**
- C. Condominium**
- D. Cooperative**
- E. Planned unit development (PUD)**
- F. Converted-use buildings**
- G. Factory-built housing**

### **IV. THE REAL ESTATE MARKET**

- A. Supply and demand**
  1. Factors affecting supply
    - a. Availability of properties in various price ranges
    - b. Construction costs (labor, materials, and fees)
    - c. Government controls and interest rates
  2. Factors affecting demand
    - a. Demographics
    - b. Employment and wage levels
    - c. Financial considerations for the homeowner

**B. Tax advantages for homeowners and investors**

- Real estate brokers should not advise on tax advantages or disadvantages but should recommend that buyers and sellers seek the advice of a qualified tax consultant.

1. Deductions allowed on a first and second residence:

- a. Property taxes (ad valorem taxes)
- b. Mortgage interest
- c. Points paid on loans used to improve or acquire
  - i. Remember \_\_\_\_\_: Points, origination fees, interest, and property taxes are deductible.
- d. Must \_\_\_\_\_ to take the deduction on tax return

**C. Capital gains**

1. Short-term gain: Property held 12 months or less is taxed at ratepayer's ordinary income tax rate.
2. Long-term gain: Property held more than 12 months is taxed at a different rate than ordinary income.
3. Salespersons and brokers should recommend that buyers and sellers seek tax advice.

**D. Taxation of gain on sale of principal residence**

1. Gain from the sale of a principal residence is excluded from tax.
  - a. \_\_\_\_\_ maximum if single taxpayer
  - b. \_\_\_\_\_ maximum if married and filing jointly
2. The taxpayer must own and occupy for at least \_\_\_\_\_ years preceding the sale.
  - a. The occupancy does not have to be sequential.

## UNIT 1 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

\$250,000	market value	property taxes
\$500,000	mortgage interest	real estate broker
a client for a fee	opinion	real estate brokerage firm
brokerage	person or company	real estate licensees
continuing education	points	renew
five	prelicensing	two
liquidity	property manager	

- The business of bringing people together in a real estate transaction is known as \_\_\_\_\_.
- A broker/brokerage/firm is a \_\_\_\_\_ licensed to perform brokerage services for \_\_\_\_\_.
- Only a brokerage firm may employ \_\_\_\_\_ to perform real estate services on behalf of the brokerage.
- Buyers, sellers, landlords, and tenants hire a \_\_\_\_\_, not salespersons or broker-associates, for real estate services and agency representation.
- A licensed appraiser's job is to develop an \_\_\_\_\_ of a property's \_\_\_\_\_, based on established methods and the appraiser's professional judgment.
- The sale of a primary residence is exempt from capital gains tax until the gain exceeds \_\_\_\_\_ for single taxpayers or \_\_\_\_\_ for married taxpayers filing jointly, provided they occupied the residence for at least \_\_\_\_\_ of the last \_\_\_\_\_ years.
- A real estate asset generally lacks \_\_\_\_\_, meaning it can take a long time to sell and thus to convert equity into cash.
- Prelicensing education is required to obtain a license, and \_\_\_\_\_ is required to renew a license.
- A property manager may be required to be a licensed \_\_\_\_\_.
- A rental property owner can hire a brokerage firm as \_\_\_\_\_ to maintain and manage property on behalf of the property owner.

## UNIT 1 GLOSSARY REVIEW ANSWERS

1. brokerage
2. person or company, a client for a fee
3. real estate licensees
4. real estate brokerage firm
5. opinion, market value
6. \$250,000, \$500,000, two, five
7. liquidity
8. continuing education
9. real estate broker
10. property manager



# UNIT 1 QUIZ

---

1. The business of bringing people together in a real estate transaction is known as
  - A. real estate brokerage.
  - B. appraisal.
  - C. real estate counseling.
  - D. property management.
2. The process of developing an opinion of a property's value (typically, market value) based on established methods and a professional judgment is
  - A. appraisal.
  - B. home inspection.
  - C. appreciation.
  - D. property certification.
3. A homeowner sold the house that she owned by herself and had a capital gain of \$175,000. To exclude that gain from her income for tax purposes, she must
  - A. be at least 55 years old.
  - B. have lived in the house for three years.
  - C. have lived in the house for two of the last five years.
  - D. have lived in the house for two of the last three years.
4. What can a homeowner deduct from income taxes?
  - A. Points, interest, and homeowners association (HOA) dues
  - B. Taxes, points, and insurance
  - C. Origination fees, points, interest, and taxes
  - D. Points, insurance, taxes, and interest
5. To deduct items on personal income tax, the taxpayer
  - A. should have the form prepared by an accountant.
  - B. must use an itemized form.
  - C. may deduct only those items that apply to the taxpayer's primary residence.
  - D. must determine whether a gain was made before filing.
6. A homeowner who does not want to be responsible for exterior property maintenance should consider purchasing a
  - A. detached single-family residence.
  - B. multi-unit structure.
  - C. factory-built home.
  - D. condominium.
7. Who do clients hire for representation in real estate transactions?
  - A. Brokerage firm
  - B. Salesperson
  - C. Sales associate
  - D. Provisional broker
8. The terms *real estate agent*, *licensee*, and *real estate professional* generally refer to
  - A. real estate brokerage firms.
  - B. licensed brokers.
  - C. real estate salespersons.
  - D. all of these.
9. Which of the following statements is TRUE regarding real estate professionals?
  - A. Real estate professionals generally must be licensed in each state in which they practice.
  - B. Real estate professionals must be residents of any state in which they are licensed.
  - C. Once licensed in their home state, real estate professionals may practice anywhere in the United States.
  - D. Real estate professionals may practice real estate only in reciprocal states.
10. Real estate brokerage activities include charging a fee for helping others
  - A. buy property.
  - B. sell property.
  - C. manage property.
  - D. do all of these.
11. A real estate broker/brokerage/firm
  - A. is a person or a company.
  - B. is licensed to charge clients a fee for brokerage services.
  - C. may employ real estate licensees.
  - D. is all of these.

12. To act as an appraiser, a real estate professional must obtain a license issued by which entity?
  - A. The federal government
  - B. A local municipality
  - C. The state
  - D. The county
13. Which phrase BEST describes an appraisal?
  - A. An opinion of value
  - B. A home inspection
  - C. A purchase contract
  - D. A mortgage
14. A real estate brokerage hired to maintain and manage property on behalf of the property owner is
  - A. a property manager.
  - B. a salesperson.
  - C. an appraiser.
  - D. an associate broker.
15. Which type of license may be required to manage a property for another and for a fee?
  - A. Real estate broker
  - B. Real estate salesperson
  - C. Associate broker
  - D. Appraiser
16. Which licensee works with borrowers seeking a mortgage loan to buy a home?
  - A. Mortgage loan originator (MLO)
  - B. Real estate salesperson
  - C. Appraiser
  - D. Property manager
17. Commercial real estate includes all of the following land uses EXCEPT
  - A. single- and multifamily housing.
  - B. office buildings.
  - C. retail facilities.
  - D. parking structures.
18. Commercial and residential uses in the same building or development is known as which type real estate?
  - A. Mixed use
  - B. Special purpose
  - C. Commercial
  - D. Residential

# UNIT 1 BROKER-LEVEL QUESTIONS

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1. A married couple has lived in their primary home for 10 years. One spouse was recently transferred to another state, and the couple would like to rent their home because they hope to return to the area in the future. If the couple decide to sell their home later, how many years may they rent the house and still qualify for the capital gain exclusion on the sale?
  - A. Zero years
  - B. Three years
  - C. Five years
  - D. Six years
2. The real estate market is primarily affected by the monetary policies of
  - A. major banks and other lenders.
  - B. brokerage firms.
  - C. state governments.
  - D. the Federal Reserve Board (the Fed).

# UNIT 1 QUIZ ANSWERS

---

1. **A** The answer is real estate brokerage. Brokerage is conducted by a real estate broker (a person or company licensed to buy, sell, exchange, or lease real property for others and for compensation) or by a real estate salesperson (sales associate) who conducts brokerage activities on behalf of the broker.
2. **A** The answer is appraisal. Licensed appraisers use established and regulated methods of valuation to estimate a property's value.
3. **C** The answer is have lived in the house for two of the last five years. Homeowners may exclude gain from the sale of a principal residence they have lived in for two of the last five years. The maximum exclusion is \$250,000 for a single person.
4. **C** The answer is origination fees, points, interest, and taxes. Remember POIT: points, origination fees, interest, and taxes can be deducted. HOA dues and principal payments are not deductible from income taxes.
5. **B** The answer is must use an itemized form. Itemized tax forms must be used to obtain deductions, such as depreciation.
6. **D** The answer is condominium. A condominium building's exterior and other common elements will be maintained by the condominium association.
7. **A** The answer is brokerage firm. Only brokerage firms are allowed to enter into agency agreements with clients. Licensees act on behalf of the brokerage firm that employs them.
8. **D** The answer is all of these. Terms such as *real estate agent*, *licensee*, and *professional* generally refer to anyone or any entity holding a real estate license, such as licensed real estate firms, brokers, and salespersons.
9. **A** The answer is real estate professionals generally must be licensed in each state in which they practice, unless the states have a reciprocal licensing arrangement.
10. **D** The answer is do all of these. Anyone who, for a fee, assists another to buy, sell, or lease property must be a real estate licensee associated with a real estate firm.
11. **D** The answer is all of these. The size of a brokerage firm may range from a small business, such as a sole proprietorship, up to a large corporation.
12. **C** The answer is the state. Appraisal licenses are issued by the state. Like real estate agents, appraisers can be licensed in more than one state.
13. **A** The answer is an opinion of value. An appraisal is the process of developing an opinion of a property's market value, based on established methods and the appraiser's professional judgment.
14. **A** The answer is a property manager. Only licensed real estate brokers may manage a property for another and for a fee.
15. **A** The answer is real estate broker. A property manager may need to be a licensed real estate broker in the state where the property is located. Depending on the state, a property manager license may be required. It is important to understand the state's requirements when it comes to property management.
16. **A** The answer is mortgage loan originator (MLO). MLOs are registered with the Nationwide Multistate Licensing System (NMLS) and licensed in the state in which they practice.

17. **A** The answer is single- and multifamily housing. Residential real estate generally includes any real estate where people live for a long term. Hotels are considered commercial real estate.
18. **A** The answer is mixed use. Mixed-use property includes various property types in a single building or development. Mixed-use developments often include office, retail, entertainment, and residential buildings.

### Broker-Level Questions

1. **B** The answer is three years. The couple must occupy the home for two out of the last five years, so they may rent it for three years and then sell without paying gains. If they rent it for longer, then they would have to return to living in the home as a primary residence to meet the occupancy requirement.
2. **D** The answer is the Federal Reserve Board (the Fed). The Fed establishes a discount rate of interest for the money it lends to commercial banks, resulting in a direct impact on the rate charged by the banks to borrowers.



# UNIT 2

## Real Property and the Law

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the concepts of land and ownership rights in real and personal property.
- › Discuss the limitations of the real estate professional under the law.

### KEY POINTS—UNIT 2

- There are two types of property: real property and personal property.
- Real estate is the land plus improvements to the land that are permanently attached to it.
- Real property can be defined as the rights, interests, and benefits included in the ownership of real estate. Most states consider the terms *real estate* and *real property* to be synonymous. Real property is conveyed by deed.
- Personal property (chattel) is everything that is not attached to the land, and it may or may not be conveyed when the property is sold. Personal property is conveyed by a bill of sale.
- Rights and interests in the land include surface, subsurface, and air rights. Improvements may be natural (growing) or human-made (fixtures). Personal property attached to the improvements becomes a fixture. Land is not classified as a fixture.
- The tests for distinguishing fixtures from personal property include the method of attachment, adaptation of the item to the property, the relationship of the parties, the intention of the person in placing the item on the land, and the agreement of the parties. Fixtures are considered real property and are conveyed in the deed. Trade fixtures used by a business are usually owned and installed by a tenant for the tenant's use and are removable.

## I. LAND, REAL ESTATE, AND REAL PROPERTY

### A. Key points

1. Real estate is defined as the land *plus* all human-made improvements (appurtenances) that are permanently attached (annexed) to the land.
2. Real estate is immovable.
  - a. When a property is sold, the land and all improvements and rights of ownership automatically transfer to the new owner via a deed.

### B. Land

1. \_\_\_\_\_ rights
2. \_\_\_\_\_ rights
3. \_\_\_\_\_ rights

### C. Improvements

1. Items \_\_\_\_\_ with the intent of \_\_\_\_\_
  - a. Examples: \_\_\_\_\_, \_\_\_\_\_, road, landscaping (such as roses, grapes, or other perennials)

### D. Rights to real property

1. Three forms of rights
  - a. Land rights, such as surface, air, water, and mineral rights
  - b. Bundle of legal rights of ownership, such as the right of an owner to possess, transfer, and control the property
  - c. Government rights, such as land-use controls, taxation, eminent domain, and escheat (Unit 3)
2. Land rights
  - a. Surface rights—the entire surface of the land
  - b. Air rights
    - i. Rights extend as high as can be legally used
    - ii. Government controls air space above



- c. Water rights—rights of water use
- i. Riparian—land abutting \_\_\_\_\_
  - ii. Littoral—land abutting \_\_\_\_\_
    - Note: Both are tied to navigation rights.
    - Ownership rights generally extend to the average high-water mark.
    - Water use rights do not automatically include the right of waterfront access to the water source. (Irrigation channels and ditches distribute water from the source.)
    - An off-waterfront owner of a water right
      - does not have the right to cross another's property to access the water source, but
      - could obtain the right of access from the waterfront owner via an easement.
  - iii. Accretion—gradual addition to land through natural causes
  - iv. Reliction—land uncovered by the receding of a navigable body of water
  - v. Erosion—gradual wearing away of the land by natural forces
  - vi. Avulsion—sudden loss of land by an act of nature
  - vii. The property line is generally maintained even if the land is no longer there.
  - viii. In states where water is scarce, ownership and use of water are often determined by the doctrine of \_\_\_\_\_.
    - The right to use water is controlled by the state rather than by the landowner adjacent to the water.
    - A landowner must demonstrate to a state agency that the owner's plans are for beneficial use, such as crop irrigation.
    - The priority of water rights is usually determined by the oldest recorded permit date.
- d. Mineral rights (subsurface rights)
- i. Transferred when property is sold unless reserved by the seller
  - ii. May be leased or sold separately from the land
  - iii. May be held by a \_\_\_\_\_
3. Real estate—transferred by a \_\_\_\_\_

## II. REAL PROPERTY VS. PERSONAL PROPERTY

### A. Personal property (chattel) key points

1. All property that is not real property
  - a. is movable,
  - b. \_\_\_\_\_ permanently \_\_\_\_\_, and
  - c. must be \_\_\_\_\_ in the purchase contract to transfer with the property.
2. Personal property is transferred by a \_\_\_\_\_.

### B. Fixture

1. An object that was once personal property that has been \_\_\_\_\_ an improvement so as to become real property
2. Land is never a \_\_\_\_\_.
3. Once the fixture (personal property) is attached, it becomes an \_\_\_\_\_ and is automatically transferred by the deed.

### C. Tests for a fixture

1. Was the object affixed or installed with the apparent \_\_\_\_\_ of improving the land?
2. Intent is evidenced by the following:
  - a. Method of attachment
    - i. Permanence of method
    - ii. \_\_\_\_\_ = fixture
    - iii. \_\_\_\_\_ = personal property
  - b. The adaptability of the item for the land's ordinary use
  - c. The agreement of the parties
    - i. The \_\_\_\_\_ is the final decision on what will be conveyed.
    - ii. Fixtures must be \_\_\_\_\_ from the purchase contract if the seller is not going to convey.

**D. Plants and trade fixtures**

1. Trees, perennial shrubbery, and grasses that do not require annual cultivation are fructus naturales and are part of the real estate.
2. Emblements, or fructus industriales, are annually cultivated crops and belong to the party who planted them, unless otherwise agreed.
3. Trade fixtures are owner- or tenant-installed additions that are a necessary part of their trade or business.
  - a. The tenant may remove trade fixtures before lease termination.
    - i. If not removed by the time of lease termination, the trade fixtures belong to the landlord.
  - b. Sale of a business property does not automatically include trade fixtures.
4. If trade fixtures or emblements are transferred, they will be transferred by a bill of sale.

**III. LAWS AFFECTING REAL ESTATE****A. Contract law****B. General property law****C. Agency law****D. Real estate license law****E. Federal, state, and local laws and regulations**

1. Consumer protection
2. Environmental
3. Tax
4. Land use
5. Zoning

## UNIT 2 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

appurtenances	emblems	littoral
bill of sale	excluded	personal property
built in	fixtures	prior appropriation
deed	freestanding	rights
do	included	riparian
do not	land	trade fixtures

1. All property other than real estate is known as \_\_\_\_\_.
2. Real estate consists of land, improvements, \_\_\_\_\_, interests, and fixtures.
3. If a seller is taking a fixture, it must have been \_\_\_\_\_ from the purchase contract.
4. Ownership of creekside rights is known as \_\_\_\_\_ rights.
5. When articles of personal property, including landscaping, are permanently attached to the improvements, they become \_\_\_\_\_.
6. Real estate and fixtures are transferred with a(n) \_\_\_\_\_.
7. Personal property is transferred with a(n) \_\_\_\_\_.
8. \_\_\_\_\_ are annually cultivated crops that belong to the party who planted them, unless otherwise agreed.
9. Owner- or tenant-installed additions that are a necessary part of their trade or business are known as \_\_\_\_\_.
10. Emblements and trade fixtures \_\_\_\_\_ automatically transfer with the deed.
11. In arid states, the right to use water for beneficial use is often determined by the doctrine of \_\_\_\_\_.
12. Fixtures such as a fireplace mantle are \_\_\_\_\_, while personal property is \_\_\_\_\_.
13. A deed transfers ownership of the land and \_\_\_\_\_.

## UNIT 2 GLOSSARY REVIEW ANSWERS

1. personal property
2. rights
3. excluded
4. riparian
5. fixtures
6. deed
7. bill of sale
8. Emblements
9. trade fixtures
10. do not
11. prior appropriation
12. built in, freestanding
13. appurtenances

# UNIT 2 QUIZ

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1. The definition of real estate includes
  - A. land.
  - B. improvements.
  - C. rights.
  - D. all of these.
2. Which of the following would ordinarily be considered personal property?
  - A. Drapery rods
  - B. Freestanding refrigerator
  - C. Built-in bookcase
  - D. Ceiling fan
3. All of the following are true about fixtures EXCEPT
  - A. fixtures typically start as personal property.
  - B. if the seller is going to keep a fixture, it must be excluded in the purchase contract.
  - C. trade fixtures are treated the same as all other fixtures.
  - D. the intention, attachment, adaptation, and agreement are all used to define a fixture.
4. A tenant installed shelving as a part of her business. At the conclusion of the lease, the tenant
  - A. may remove the shelving only if she reimburses the landlord.
  - B. must leave the shelving because it is the landlord's property.
  - C. may remove the shelving and is not required to reimburse the landlord.
  - D. must leave the shelving but may demand that the landlord reimburse her.
5. All of the following are considered fixtures EXCEPT
  - A. plumbing.
  - B. wiring.
  - C. grapevines.
  - D. draperies.
6. The principle of the doctrine of prior appropriation determines
  - A. which user's water rights have priority.
  - B. who owns the fixtures.
  - C. how personal property is distributed.
  - D. who has access to water rights.
7. All of the following apply to water rights EXCEPT
  - A. riparian rights.
  - B. littoral rights.
  - C. avulsion.
  - D. appurtenant.
8. Which of the following is TRUE about mineral rights?
  - A. They represent an interest in personal property.
  - B. They often are held by a third party.
  - C. They always belong to the state.
  - D. Liquid minerals are considered personal property.
9. A *fixture* is defined as
  - A. personal property attached to real property.
  - B. a lien of record.
  - C. chattel.
  - D. an encumbrance.
10. A seller and buyer have negotiated an offer back and forth. In the original offer, the buyer asked for the seller's installed hot tub, which the seller had excluded from all marketing, the multiple listing service (MLS) listing, and the listing contract. In the final accepted offer, the hot tub is not mentioned. Who will own the hot tub at closing?
  - A. The seller, because the seller gave notice in the marketing and MLS listing, and the listing broker was aware of the exclusion
  - B. The buyer, because the hot tub is automatically transferred with the property because it is personal property
  - C. The buyer; the seller would be in breach if the hot tub were to be removed
  - D. The seller, because it was excluded in the listing

11. The sellers wish to keep their prized rose bushes for transplant to their new property. Which statement is the MOST accurate?
  - A. The rose bushes are fixtures that the sellers must exclude from the purchase contract.
  - B. Landscaping is considered personal property and is not included with the sale.
  - C. Sellers are not allowed to exclude any fixtures from the sale.
  - D. Ownership of fixtures is determined by prior appropriation.
12. The opposite of erosion is BEST described as
  - A. avulsion.
  - B. irrigation.
  - C. accretion.
  - D. mitigation.
13. Waterfront property ownership rights generally extend to
  - A. the center of the lake or river.
  - B. the line of prior appropriation.
  - C. the opposite shoreline.
  - D. the average high-water mark.
14. Real estate is defined as the land plus appurtenances. Appurtenances include all of the following EXCEPT
  - A. improvements.
  - B. personal property.
  - C. rights.
  - D. fixtures.

# UNIT 2 BROKER-LEVEL QUESTIONS

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1. All of the following are fixtures that may not be removed from a property without exclusion in the real estate contract EXCEPT
  - A. fireplace tools.
  - B. rose bushes.
  - C. an installed spa.
  - D. storm doors.
2. Which of the following would have to be included in a purchase contract if the owner wanted to convey them to a buyer?
  - A. Drapery rods and built-in shelving
  - B. Dishwasher and garbage disposal in the kitchen
  - C. Rose bushes and grapevines
  - D. Custom-built freestanding bookcase



# UNIT 2 QUIZ ANSWERS

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1. **D** The answer is all of these. Real estate includes the land and appurtenances, such as improvements, rights, interests, and fixtures.
2. **B** The answer is freestanding refrigerator. Personal property is not permanently attached to real estate.
3. **C** The answer is trade fixtures are treated the same as all other fixtures. Trade fixtures are considered personal property and transferred by a bill of sale.
4. **C** The answer is may remove the shelving and is not required to reimburse the landlord. Shelving is an example of a trade fixture. Trade fixtures are the tenant's personal property and may be removed by the tenant at the conclusion of the lease.
5. **D** The answer is draperies. Draperies are considered personal property because they are not attached.
6. **A** The answer is which user's water rights have priority. The doctrine of prior appropriation determines which user's water rights have priority.
7. **D** The answer is appurtenant. Appurtenances may or may not apply to water rights, depending on state laws.
8. **B** The answer is they often are held by a third party. In a sale, if the seller retains the mineral rights and sells them separately from the surface rights, the new buyer who now holds the subsurface mineral rights is called the third party.
9. **A** The answer is personal property attached to real property. Fixtures are personal property that are attached to improvements.
10. **C** The answer is the buyer; the seller would be in breach if the hot tub were to be removed. The hot tub is a fixture and cannot be removed without the seller being in breach because the seller did not specifically exclude it in the purchase contract.
11. **A** The answer is the rose bushes are fixtures that the sellers must exclude from the purchase contract. Fixtures are appurtenances and will transfer to the new owner unless specifically excluded in the sale contract.
12. **C** The answer is accretion. Erosion is the gradual wearing away of land by water or wind. Accretion is the gradual accumulation of land by action of water depositing sediment along a shoreline.
13. **D** The answer is the average high-water mark. While dependent on state laws, property ownership rights generally end at the average high-water mark.
14. **B** The answer is personal property. Appurtenances are everything that is attached to the land: improvements, rights, interests, and fixtures. By definition, personal property is movable and not attached to the land or improvements.

## Broker-Level Questions

1. **A** The answer is fireplace tools. Fireplace tools are personal property and would need to be included in the contract to convey. All other items are fixtures and will convey without being mentioned in the deed.
2. **D** The answer is custom-built freestanding bookcase. A freestanding (i.e., not attached) bookcase is personal property and would need to be included in the sales contract to convey to a buyer.



# UNIT 3

## Interests in Real Estate

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Identify the various types of estates.
- › Explain the differences between liens and other types of encumbrances.
- › Explain the limitations that are imposed on private property rights for the welfare of the public.

### KEY POINTS—UNIT 3

- An estate is an interest in property. There are two types of estates: freehold estates of ownership and leasehold estates of possession. Freehold estates have an indefinite duration, which lasts until the property is transferred.
- A fee simple absolute estate is the greatest and maximum form of ownership.
- Fee simple defeasible ownership is a qualified fee because this type of estate always has a condition that must be met. If the deed condition is broken, the estate may revert to the grantor or the grantor's heirs.
- With a fee simple determinable, the former owner retains a possibility of reverter. With a fee simple subject to a condition subsequent, the former owner (or the owner's heir or successor) has a right of reentry if the condition is violated.
- A life estate is an estate measured by someone's lifetime. The person who will receive the property when the life estate ends holds a remainder or reversionary interest. If no remainderman is named, the estate reverts to the grantor or the grantor's heirs.
- An encumbrance is any right, claim, or interest in property held by someone other than the property owner or the one who has a legal right of possession.
- An easement is a right of use. Easements may be appurtenant or in gross. Easements may be created by express contract, necessity, or prescription. Once given, easements are not revocable.

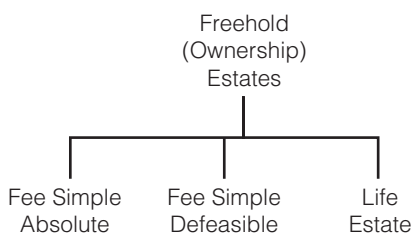
- Deed restrictions are privately created limitations on land use. They apply to present and future owners. The most common examples are restrictive covenants imposed on all lots within a subdivision by the original developer.
- A license is similar to an easement; it grants permission to enter another's property for a specific purpose. However, unlike an easement, a license does not create an interest in the property and is not an encumbrance against the title. Unlike an easement, a license can be revoked at any time.
- An encroachment is an unauthorized use of someone else's property, typically a physical object intruding onto neighboring property. Most encroachments are unintentional. A survey would reveal an encroachment.
- An individual's property rights are subordinate to government rights. The government has the power to determine land use, assess property taxes, regulate private property, and take private property for public use.
- Police power is the power that implements public controls for land use. It allows state and local governments to regulate how a property owner uses the property (e.g., through zoning laws or other land-use restrictions such as environmental limitations) for the protection of the public's health, safety, and general welfare.
- The power of eminent domain is the government's power to take private property for public use. Condemnation is the process that exercises this right. When private property is taken, the government must pay just compensation to the owner.
- General real property taxes are levied to support the general operation and services of government and create a priority lien. Profit realized in the sale of real estate is taxed. Special fees are levied for the cost of specific local improvements, and only those pieces of property that benefit from the improvement are taxed.
- If property is abandoned, or if a person dies intestate and without heirs, the property will escheat to the state.

## I. ESTATES IN LAND

### A. Freehold estates

1. An interest or right in real property
2. Types of freehold estates of ownership

**Figure 3.1: Types of Freehold Estates**



- a. Fee simple absolute—most complete bundle of rights (also known as fee estate or fee simple)
- b. Fee simple defeasible may be fee simple determinable or fee simple subject to a condition subsequent
- c. Life estate
  - i. The life tenant (grantee) is the property owner.
  - ii. Upon death of the life tenant, the estate returns to \_\_\_\_\_ and reverts to either the grantor (\_\_\_\_\_) or a third party (\_\_\_\_\_).
  - iii. The life tenant may lease or even sell the property, but upon the life tenant's death, the buyers/tenants lose their interest.
  - iv. A life estate is transferable but not inheritable.
  - v. A legal life estate is created by state law and includes a \_\_\_\_\_.

## II. ENCUMBRANCES

### A. Key points

- 1. An encumbrance is any claim, right, or interest held by a party who is \_\_\_\_\_ of the property; a nonpossessory interest.
- 2. An encumbrance is an appurtenance—it attaches to and binds real property.
- 3. An encumbrance may impact the ability of the seller to deliver marketable title.
- 4. Buyers should \_\_\_\_\_ if they have any concerns about an encumbrance.

### B. Liens

- 1. Provide \_\_\_\_\_ for a debt or obligation of the property owner
- 2. Are a charge against the property if the debt is not repaid

### C. Private restrictions on the use of real estate

- 1. Deed restrictions are \_\_\_\_\_ created controls on land use.
  - a. Created by the original property developer or subsequent owner/grantor
  - b. Provisions are placed in deeds to control future land use.
- 2. Deed restrictions are appurtenant to and run with the land.
- 3. Deed restrictions must have a \_\_\_\_\_.

**D. Easements**

1. An easement is the \_\_\_\_\_ of another and may be created by
  - a. an express contractual agreement (voluntary), or
  - b. prescription or necessity (court ordered).
2. An easement is a real property interest and is therefore transferred by deed.
3. Appurtenant easement
  - a. The \_\_\_\_\_ tenement is the property receiving the benefit of the easement.
  - b. The \_\_\_\_\_ tenement is the property encumbered by the easement.
  - c. Does not increase size of the dominant land, but may increase its value
  - d. The dominant holder doesn't own the land but has the right of use.
    - i. Examples:
      - Driveway \_\_\_\_\_ for ingress and egress
      - Party walls, shared driveways, lake access
  - e. Could grant permanent access to a neighbor's property
4. Easement \_\_\_\_\_
  - a. Commercial easement held by company, government, or person
  - b. Has no dominant property, only \_\_\_\_\_ property
  - c. A person or entity benefits
  - d. Example: \_\_\_\_\_ easement
5. Court-ordered easements
  - a. Easement by necessity
    - i. Created when an owner sells a contiguous parcel of land that has no legal access
    - ii. Granted only if there is no other access to a street or public way
    - iii. Prevents creation of landlocked property
  - b. Easement by prescription—acquired by meeting statutory requirements (Unit 6)

6. Easements can be terminated in the following ways:

- a. When the need no longer exists
- b. Merger—holder of servient property acquires the dominant property
- c. Release—holder of dominant interest releases rights to servient owner (via quitclaim deed)
- d. Abandonment—intention of parties is the determining factor
- e. Unless terminated, an easement by prescription will \_\_\_\_\_.

#### **E. Licenses**

1. A license is a \_\_\_\_\_ to use the property
  - a. Not a right to use—permission to use
  - b. Does not run with the land
  - c. Unassignable—license holder may not transfer to others

#### **F. Encroachments**

1. An encroachment is the unauthorized use of another person's land or a physical object intruding onto neighboring property.
  - a. Examples: part of a structure, fence, roof, or tree limb exceeding the property line
2. A survey will reveal encroachments.
3. An encroachment that exceeds the state's prescriptive period may give rise to an easement by prescription.

#### **G. Lis pendens**

1. A notice filed in the public record of a pending legal action
2. Creates a "cloud of title" until removed

### **III. GOVERNMENTAL POWERS**

#### **A. Police power—\_\_\_\_\_ of land**

1. Right to enact and enforce laws governing \_\_\_\_\_
2. Environmental protection laws, \_\_\_\_\_, building codes
3. Determines how land can be \_\_\_\_\_

**B. Eminent domain**

1. Right to take \_\_\_\_\_ for public use
2. Process used is called \_\_\_\_\_
3. Example of involuntary alienation—a compulsory transfer of title
4. Compensation = value plus damages

**C. Taxation**

1. Property taxes are paid to the county where the property is located
2. Special fees may be charged against specific properties that benefit from a public improvement.
  - a. Examples: paving, curbs and gutters, street lights

**D. Escheat**

1. Government's right to \_\_\_\_\_ that has been abandoned
2. Exercised when owner dies with no will (intestate) and without locatable heirs

**E. Remember the mnemonic device PETE**

1. Police power
2. Eminent domain
3. Taxation
4. Escheat



## UNIT 3 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

appurtenant	encroachment	lien
deed restrictions	encumbrance	life estate
definite duration	escheat	mechanic's lien
easement	fee simple absolute	police power
easement in gross	indefinite duration	private control
eminent domain	leasehold estate	revocable

- List two rights the government can use to acquire privately held land:
  - \_\_\_\_\_
  - \_\_\_\_\_
- A right of use or enjoyment that one person has in the land of another for a specific purpose is a(n) \_\_\_\_\_.
- A tenant's right to possess real estate for the term of a lease is a(n) \_\_\_\_\_.
- A tree limb that overhangs into a neighbor's yard is an example of a(n) \_\_\_\_\_.
- An easement is not \_\_\_\_\_, but a license is.
- A claim that one party has against the land of another to secure payment of a debt is a(n) \_\_\_\_\_.
- A person who has not been paid for work performed on real property may record a(n) \_\_\_\_\_.
- A party wall, shared driveway, or the right to cross the land of another are examples of an easement \_\_\_\_\_.
- The most complete form of ownership rights that allow an owner to occupy a parcel of real estate forever is \_\_\_\_\_.
- A freehold estate is an estate of ownership with a(n) \_\_\_\_\_.
- Deed restrictions are created as a form of \_\_\_\_\_ of land use.

## UNIT 3 GLOSSARY REVIEW ANSWERS

1. escheat, eminent domain
2. easement
3. leasehold estate
4. encroachment
5. revocable
6. lien
7. mechanic's lien
8. appurtenant
9. fee simple absolute
10. indefinite duration
11. private control

# UNIT 3 QUIZ

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1. The process by which the government exercises its power to take private land for public use is
  - A. condemnation.
  - B. escheat.
  - C. foreclosure.
  - D. eminent domain.
2. All of the following are government powers EXCEPT
  - A. deed restrictions.
  - B. taxation.
  - C. zoning.
  - D. escheat.
3. An estate refers to
  - A. the amount of property owned by an individual.
  - B. the rights held by someone who has a possessory interest in real estate.
  - C. a claim against or interest in land held by someone other than the owner of the property.
  - D. an exercise of police power.
4. When an individual or entity holds a claim against another's property, it is
  - A. an estate.
  - B. a life tenancy.
  - C. a lien.
  - D. a license.
5. All of the following are considered real property rights EXCEPT
  - A. land rights.
  - B. government rights.
  - C. natural rights.
  - D. ownership rights.
6. Which of the following would be used to reveal encroachments?
  - A. Standard title insurance
  - B. Abstract of title
  - C. Survey
  - D. Attorney's title opinion
7. A homestead is a
  - A. mechanic's lien.
  - B. life estate pur autre vie.
  - C. legal life estate.
  - D. fee simple defeasible.
8. The grantor of a life estate retains
  - A. a leasehold estate.
  - B. a qualified fee estate.
  - C. a right of remainder.
  - D. a reversionary interest.
9. If Ann grants a life estate to Ben and specifies that title will be transferred to Carl on the death of Ben, which of the following is FALSE?
  - A. Ben is the life tenant.
  - B. Carl has a reversionary interest.
  - C. Ben owns the property.
  - D. Carl is the remainderman.
10. Life tenants in most life estates have all of the following rights EXCEPT
  - A. they may place the property in their will.
  - B. they can sell the property.
  - C. they can lease the property.
  - D. they may improve the property.
11. All of the following could be encumbrances on real estate EXCEPT
  - A. a lien.
  - B. an easement.
  - C. a deed restriction.
  - D. a fixture.
12. An estate that lasts only so long as a specified condition is met is known as
  - A. a life estate.
  - B. a defeasible fee.
  - C. a fee simple absolute.
  - D. a deed restriction.
13. The right of the government to establish zoning and land-use laws is an exercise of which of the following?
  - A. Police power
  - B. Escheat
  - C. Government survey
  - D. Eminent domain

14. The grantor of a defeasible fee has set the requirement that the property “must be used only as a school.” This requirement is known as
  - A. a blue law.
  - B. a remainder interest.
  - C. a reversionary interest.
  - D. a deed condition.
15. Which government right is exercised when the state acquires private property through condemnation and pays just compensation?
  - A. Escheat
  - B. Police power
  - C. Taxing power
  - D. Eminent domain
16. A holder of a life estate has all of the following interests EXCEPT
  - A. title.
  - B. ownership.
  - C. possession.
  - D. remainder.
17. An irrevocable right to use the lands of another is called
  - A. escheat.
  - B. a license.
  - C. an encroachment.
  - D. an easement.
18. A holder of a freehold estate has rights of
  - A. escheat.
  - B. illegal use.
  - C. ownership.
  - D. domain.
19. Which is NOT an estate of ownership?
  - A. Estate for years
  - B. Life tenancy
  - C. Fee simple
  - D. Qualified fee
20. All of the following would be considered to have an interest in land EXCEPT
  - A. a farmer who is leasing 20 acres.
  - B. the holder of an easement.
  - C. a hunter who has been given permission to hunt in a field.
  - D. a lender holding a mortgage lien.
21. The property Sam bought 30 years ago had an appurtenant easement for access. Then, 20 years ago, the county built a new road, and Sam has not used the easement since that time. When Sam sells the property, the easement
  - A. will automatically return to the servient property owner.
  - B. will no longer run with the land due to the statute of limitations.
  - C. must be renewed by rerecording it with the county.
  - D. remains in place and will transfer with the property.
22. Protection on a primary home against certain creditors is known as
  - A. specific lien rights.
  - B. homestead rights.
  - C. general lien rights.
  - D. deed restrictions.
23. A property owner passed away, having no heirs and leaving no will. Ownership of the property may revert to the state through the government’s right of
  - A. escheat.
  - B. police power.
  - C. eminent domain.
  - D. taxation.
24. Public restrictions on private land use is an example of
  - A. eminent domain.
  - B. police power.
  - C. escheat.
  - D. taxation.
25. Private restrictions on private land use are BEST described as
  - A. zoning.
  - B. liens.
  - C. deed restrictions.
  - D. eminent domain.

# UNIT 3 BROKER-LEVEL QUESTIONS

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1. An heir holds the reversionary interest in a defeasible fee estate. The deceased gave the city the family home to use to house the mayor. The heir just saw on the news that the city is going to sell the home. The heir
  - A. may need to sue the city to have the property returned to the family because the deed condition is being broken.
  - B. will automatically become the owner of the property upon the sale.
  - C. has no rights because it was the deceased who created the condition.
  - D. has no recourse because the property is now government owned.
2. Escheat is BEST defined as
  - A. property taken through a condemnation process.
  - B. the process used to determine land use.
  - C. the state's right to take abandoned property.
  - D. the right to take property if the owner is paid fair compensation.
3. Eminent domain is BEST defined as
  - A. the government's right to take private property by paying fair compensation.
  - B. condemnation to take private property without paying compensation.
  - C. the public right to take abandoned property and give it to private citizens.
  - D. the private right to take private property that is abandoned through condemnation.
4. A married couple has been granted the right to occupy and use a 10-acre tract of land forever. Which of the following does the couple hold?
  - A. Fee simple estate
  - B. Estate for years
  - C. Life estate
  - D. Leasehold estate
5. A homeowner may be allowed protection from the judgments of unsecured creditors as a result of a state's
  - A. homestead rights.
  - B. littoral rights.
  - C. prior appropriation rights.
  - D. fee simple rights.

# UNIT 3 QUIZ ANSWERS

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1. **A** The answer is condemnation. The process is condemnation; the power is eminent domain.
2. **A** The answer is deed restrictions. Deed restrictions are private restrictions on the use or sale of a property.
3. **B** The answer is the rights held by someone who has a possessory interest in real estate. An estate in land refers to the collection or bundle of rights held by someone who has a possessory interest in a piece of real estate.
4. **C** The answer is a lien. A lien secures repayment of indebtedness.
5. **C** The answer is natural rights. Real property rights are those of land, government, and ownership, not natural rights.
6. **C** The answer is survey. A survey would be used to discover zoning setback violations or encroachments.
7. **C** The answer is legal life estate. In states that have homestead exemption laws, a portion of the land or property value is exempt from certain judgments for debts.
8. **D** The answer is a reversionary interest. If the grantor of a life estate retains reversionary rights, ownership in fee simple reverts to the grantor at the end of the life estate.
9. **B** The answer is Carl has a reversionary interest. A reversionary interest could only be held by Ann, the grantor.
10. **A** The answer is they may place the property in their will. Most life estates terminate upon the death of the life tenant and therefore cannot be willed. (There is one exception—a life estate *pur autre vie*, in which the life of someone other than the life tenant is used as the measuring life.) A life tenant who sells or leases the estate has sold or leased the property for only the lifetime of the life tenant.
11. **D** The answer is a fixture. A fixture is real estate. Liens, easements, and restrictive covenants are encumbrances.
12. **B** The answer is a defeasible fee. A fee simple defeasible estate lasts so long as a deed condition is met.
13. **A** The answer is police power. Police power is the government's right to enact and enforce ordinances to foster land-use compatibility and protect the health, safety, and general welfare of the public (including land-use laws).
14. **D** The answer is a deed condition. Deed conditions are used to create the requirements of defeasible fee estates. Blue laws are state laws that prohibit sales of liquor and other items on Sunday.
15. **D** The answer is eminent domain. Condemnation is the process by which the government exercises its right of eminent domain.
16. **D** The answer is remainder. A life tenant owns the property; therefore, the life tenant has title and possession. The remainder estate belongs to the party who will obtain title upon death of the measuring life.
17. **D** The answer is an easement. Easements are nonrevocable rights to use the property of another for a specific use.
18. **C** The answer is ownership. Freehold estates are estates of ownership, which have an indefinite duration.
19. **A** The answer is estate for years. An estate for years is a leasehold right of possession, not ownership. Life tenancy, like all other freehold estates, is an estate of ownership.

20. **C** The answer is a hunter who has been given permission to hunt in a field. Granting permission to use one's land creates a license, which is not an interest in land. A license grants revocable permission to use.
21. **D** The answer is remains in place and will transfer with the property. Easements can be terminated by release, merger, or abandonment. If an easement is abandoned and the property owner wants to have it returned, typically the servient property must prove abandonment in court.
22. **B** The answer is homestead rights. Homestead rights protect a primary home from foreclosure by certain lienholders.
23. **A** The answer is escheat. If an owner dies with no familial heirs and no will to provide direction on what to do with the property, the property is abandoned and may revert to the state.
24. **B** The answer is police power. Police power is the government's right to pass ordinances controlling land use.
25. **C** The answer is deed restrictions. Deed restrictions are rules that are generally created by the project developer, with the intent to create or preserve a certain look in the development.
2. **C** The answer is the state's right to take abandoned property. Escheat is the government's right to take property that has been abandoned because the owner dies without a will or locatable heirs.
3. **A** The answer is the government's right to take private property by paying fair compensation. Eminent domain is the government's right to take private property for public use. The government must pay fair compensation. The process used is condemnation.
4. **A** The answer is fee simple estate. The right to occupy and use land forever is a fee simple estate.
5. **A** The answer is homestead rights. A homestead is land that is owned and occupied as a family home. In many states, homestead rights protect or exempt a portion of the area or value of the land from judgments or debts. While homestead law will protect a homestead from unsecured creditors such as credit card companies, it will not protect against creditors holding specific liens, such as property tax and mortgage liens.

### Broker-Level Questions

1. **A** The answer is may need to sue the city to have the property returned to the family because the deed condition is being broken. If the city tries to sell the property, the heir has the right to request that it be returned to the family because the deed condition has been broken. It may take a court action for this to happen.





# UNIT 4

## Forms of Real Estate Ownership

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Distinguish between ownership in severalty and co-ownership.
- › Describe the various forms of co-ownership in real estate.
- › Describe the key elements of trusts, partnerships, corporations, and limited liability corporations (LLCs).
- › Identify the types of property ownership for common-interest properties.

### KEY POINTS—UNIT 4

- When title to real property is held by one person or entity, it is called ownership in severalty. Property may be owned solely by one individual or by a single entity (a corporation, partnership, limited liability company, or real estate investment trust).
- Concurrent ownership or co-ownership exists when two or more people simultaneously share ownership of one piece of property. The two most common forms of co-ownership are tenancy in common and joint tenancy.
- In many states, unless an agreement exists to the contrary, co-ownership is presumed to be a tenancy in common. With a tenancy in common, there is an equal right of possession, but each tenant may hold unequal shares of ownership, and there is no right of survivorship.
- With a joint tenancy, each tenant must have an equal ownership share and equal right of possession. Joint tenants also have a right of survivorship. This means that when a joint tenant dies, his share of ownership in the property automatically passes to the surviving joint tenant(s).
- Common interest communities include condominiums, town houses, cooperatives, time-shares, and planned communities. Sales of these types of properties are generally regulated under an individual state's common interest ownership act.
- The owner of a condominium unit owns the unit, plus an undivided interest in the common elements as a tenant in common with the other unit owners.
- A cooperative, by comparison, is a building owned by a corporation. Each resident owns shares of stock in the corporation and has a proprietary lease in the individual unit.

## I. OWNERSHIP IN SEVERALTY VS. CO-OWNERSHIP

### A. Sole ownership/estate in severalty

1. Ownership by \_\_\_\_\_ is ownership in severalty.
2. Upon death, the property goes to the \_\_\_\_\_.
3. A legal entity can own in severalty.
  - a. The entity owns the property; the owners of the entity do not.
  - b. Two or more people or firms joining together as an entity is syndication.
    - i. Examples: corporation, partnership, trust, real estate investment trust (REIT)
  - c. In a general partnership, all partners have equal say and liability.
  - d. In a limited partnership, the limited partners' liability is \_\_\_\_\_.
  - e. The sale of interests may require a securities license.

## II. FORMS OF CO-OWNERSHIP

### A. Tenancy in common

1. Co-ownership by more than one person or entity
2. Definition
  - a. In concurrent (multiple) ownership, two or more parties share ownership with \_\_\_\_\_.
  - b. Their shares or interests are \_\_\_\_\_ but undivided.
  - c. Each has equal rights of possession to the entire property, but tenants in common may have unequal shares.
  - d. No co-owner has a right to any specific part of the property.
  - e. The form of co-ownership determines what happens upon the death of a co-owner.
  - f. With a tenancy in common, a deceased co-owner's interest goes to that individual's heirs or devisees.
  - g. Buyers should obtain \_\_\_\_\_ to determine the most appropriate form of co-ownership.

**B. Joint tenancy**

1. Co-owners have the \_\_\_\_\_.
2. Upon death, interests go to the co-owner(s) without going \_\_\_\_\_.
  - a. \_\_\_\_\_ a will
  - b. Death certificate and joint tenancy affidavit must be recorded.
3. The co-owners must be specified in the deed \_\_\_\_\_
4. Ownership shares must be equal.
5. Must have four unities
  - a. Possession, interest, title, and time (\_\_\_\_\_)
6. A partition lawsuit can divide property among the co-owners.

**C. Ownership by married couples**

1. Tenancy by the entirety is a form of ownership available exclusively to \_\_\_\_\_ couples in several states.
2. Some states classify property acquired after marriage as community or marital property.
3. Tenancy by the entirety, marital property, and community property are similar to joint tenancy.

**III. TRUSTS AND BUSINESS ORGANIZATIONS****A. Definition**

1. A trust allows a person to transfer ownership of property to someone else to hold or manage for the benefit of a third party.
2. The owner of the property placed in a trust is the trustor, the individual or entity that holds the trust is the trustee, and the party that ultimately obtains the benefit of the trust is the beneficiary.
3. Most states allow real estate to be held \_\_\_\_\_.

**B. Living and testamentary trusts**

1. A trust created during the property owner's lifetime is a \_\_\_\_\_.
2. A trust established by will that will take effect upon the owner's death is a \_\_\_\_\_.

**C. Land trusts**

1. Real estate is the only asset of a land trust.
2. Frequently created for the conservation of farmland, forests and other wildlife habitats, coastal land, and scenic vistas
3. Public records usually do not name the \_\_\_\_\_.

**D. Ownership of real estate by business organizations**

1. A partnership is an association of two or more persons who carry on a business for profit as co-owners.
  - a. In a \_\_\_\_\_, all partners participate in the operation and management of the business.
  - b. In a \_\_\_\_\_, there are one or more general partners who manage the business and \_\_\_\_\_ who are not legally permitted to participate but who are liable for business losses only up to the amount invested.
2. A corporation is a legal entity created under the laws of the state from which it receives its \_\_\_\_\_.
3. In a limited liability company, investors enjoy the limited liability offered by a corporation but the tax advantages of a \_\_\_\_\_.

**IV. CONDOMINIUMS, COOPERATIVES, AND TIME-SHARES****A. Condominium**

1. Real estate, portions of which are designated for
  - a. separate ownership (\_\_\_\_\_), and
  - b. the remainder is designated for common use and ownership (\_\_\_\_\_).
2. Any type or use of real estate (i.e., residential, commercial) can be a common interest community.
3. Created by recording a declaration that describes the legal and physical structure, along with any restrictions on use
  - a. Specifies common and limited common elements
  - b. Common elements are owned by all unit owners as \_\_\_\_\_.
  - c. \_\_\_\_\_ elements are owned by all and used by one. Examples include assigned parking spaces, storage units, and balconies.

4. Each unit owner is required to be a \_\_\_\_\_ of the homeowners association (HOA), \_\_\_\_\_ organization with the following functions:
  - a. Manages common elements and pays any taxes owed by the HOA
  - b. Adopts rules, regulations, and budgets
  - c. Adopts and amends bylaws (how the association operates)
  - d. Imposes and collects assessments (association fees)
    - i. Enforced by a lien on the unit
    - ii. Unpaid dues create a specific lien, which can be foreclosed by the HOA
  - e. Holds annual meeting
  - f. Maintains insurance on common elements (contents of units are not covered)
  - g. Sets rules for rentals
  - h. Does not develop land
5. Owners \_\_\_\_\_ their individual units.
6. A unit seller is required to give the buyer full disclosure, including the declaration, bylaws, HOA financial reports, and so on.

## **B. Cooperative**

1. Owned by a corporation, which in turn allows owners (stockholders) occupancy
2. A cooperative corporation (tenants' association) owns the real estate.
3. Buyer receives
  - a. membership in association,
  - b. \_\_\_\_\_, and
  - c. proprietary lease.
    - i. \_\_\_\_\_; no ownership of unit
4. Stockholder/tenant pays assessments and association fees.

**C. Time-share**

1. Purchaser buys interest in real estate and receives right to use property for certain periods of time.
2. Purchasers may own land, or developer may own land and contract for its use.
3. Purchasers of units own as tenants in common with other purchasers.
4. Most common in \_\_\_\_\_
5. Sale of a time-share or condominium with a mandatory rental pool agreement may require a securities license.

## UNIT 4 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

association	equal	severalty
common elements	homeowners association	shared
common interest	joint tenancy	tenants in common
cooperative	limited common elements	time-share
declaration	overrides	unequal
do	proprietary lease	unit
do not	right of survivorship	will

- Property owned by one person or entity is said to be owned in \_\_\_\_\_.
- A form of concurrent ownership in which each tenant owns an undivided ownership share in the entire property and has no right of survivorship is \_\_\_\_\_.
- A form of concurrent ownership in which all owners have equal shares in the property and the right of survivorship is \_\_\_\_\_.
- An undivided interest in a resort condominium as a tenant in common for a specific period each year is a(n) \_\_\_\_\_.
- \_\_\_\_\_ does not require co-owners to go through probate to obtain title, because joint tenancy with right of survivorship overrides a(n) \_\_\_\_\_.
- A person who holds a proprietary lease and owns shares of stock in a corporation that owns the building is someone who owns a(n) \_\_\_\_\_.
- Tenancy in common ownership allows for \_\_\_\_\_ shares of ownership.
- In joint tenancy, the co-owners have the \_\_\_\_\_, meaning that upon the death of one of the co-owners, the deceased co-owner's share is automatically transferred to the surviving co-owners.
- Tenants in common co-owners \_\_\_\_\_ have the right of survivorship.
- Condominiums are created by recording a(n) \_\_\_\_\_.
- The roof, swimming pool, structure, hallways, and elevators in a condominium complex are \_\_\_\_\_, which means they are owned by all and used by all.
- Condominium features such as balconies and storage lockers are \_\_\_\_\_, which are owned by all and used by one.
- A condominium owner holds a sole and separate freehold interest in the \_\_\_\_\_, plus \_\_\_\_\_ ownership of the common elements as a tenant in common.
- Condominiums, cooperatives, and planned unit developments (PUDs) are \_\_\_\_\_ communities.
- All condominium owners are required to be members of the \_\_\_\_\_, which collects dues and manages the common elements.

## UNIT 4 GLOSSARY REVIEW ANSWERS

1. severalty
2. tenants in common
3. joint tenancy
4. time-share
5. Joint tenancy, will
6. cooperative
7. unequal
8. right of survivorship
9. do not
10. declaration
11. common elements
12. limited common elements
13. unit, shared
14. common interest
15. homeowners association



# UNIT 4 QUIZ

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1. Ownership in severalty refers to
  - A. more than one owner.
  - B. the right of survivorship.
  - C. ownership between spouses.
  - D. ownership by one person or entity.
2. Which must always be TRUE of tenants in common?
  - A. Each tenant must have an equal ownership share.
  - B. Each tenant rents their share of the land from the other co-owners.
  - C. Each tenant has the right of survivorship.
  - D. Each tenant owns an undivided interest in the property.
3. A couple wants to buy a house together. If either one should die, they want the deceased's share to go to that person's heirs, not the co-owner. If the state permits it, which form of ownership allows for this option?
  - A. Tenancy in common
  - B. Tenancy by the entirety
  - C. Joint tenancy
  - D. Estate in severalty
4. Parents and their only child buy a property together. If one dies, their share of title will automatically pass to the other owners. How did they take title?
  - A. Joint tenants
  - B. Tenants in severalty
  - C. Tenants by the entirety
  - D. Tenants in common
5. All of the following are functions of homeowners associations EXCEPT
  - A. to establish budgets.
  - B. to set assessment rates for the maintenance of common elements.
  - C. to create rules for rental units if allowed in the association.
  - D. to develop and construct new units.
6. The form of ownership in which the owners own and finance their individual unit plus own a share of common elements is called
  - A. a condominium.
  - B. a general partnership.
  - C. a cooperative.
  - D. a limited partnership.
7. In a limited partnership, the limited partner's liability is
  - A. the same as all the other partners.
  - B. limited to whatever amount the general partners deem appropriate.
  - C. the same as all the other general partners' liability.
  - D. limited to the amount of the limited partner's investment in the partnership.
8. The common elements in a condominium are owned by
  - A. all the members of the HOA as joint tenants.
  - B. all former and current unit owners as tenants in common.
  - C. the HOA and current shareholders in severalty.
  - D. all current owners as tenants in common.
9. A married couple asked a real estate salesperson for advice about the best option for them to take title. The salesperson may
  - A. recommend joint tenancy, which is the preferred choice for married couples.
  - B. explain the choices and recommend joint tenancy.
  - C. tell the couple it is their decision because the salesperson cannot recommend or describe any tenancy.
  - D. describe the choices and, if the couple is still undecided, recommend they speak to an attorney or financial planner.

10. An ownership interest in real estate wherein a purchaser receives the right to use the property for certain periods of time is
  - A. a tenancy in common.
  - B. a joint tenancy.
  - C. a leasehold.
  - D. a time-share.
11. Where are time-shares MOST common?
  - A. Resort and vacation properties
  - B. Agricultural land
  - C. Suburban mixed-use developments
  - D. Urban single-family homes
12. The purchaser of a cooperative living unit does NOT receive
  - A. a proprietary lease.
  - B. a deed.
  - C. a share of stock.
  - D. a membership in the cooperative association.
13. Condominium owners are required to do all of the following EXCEPT
  - A. belong to the homeowners association.
  - B. pay association dues.
  - C. attend the annual homeowners association meeting.
  - D. follow association rules and regulations.
14. Which of the following is LEAST likely to be a common interest community?
  - A. Single-family home subdivision
  - B. Cooperatives
  - C. Condominiums
  - D. Agricultural property
15. Common elements in a condominium complex include
  - A. the exterior roofing and siding.
  - B. hallways, elevators, and social rooms.
  - C. pools, tennis courts, and other amenities.
  - D. all of these.
16. A condominium owner's balcony and storage unit are BEST described as
  - A. common elements.
  - B. owned in severalty by the unit owner.
  - C. limited common elements.
  - D. encumbrances.
17. Which of these BEST describes condominium ownership?
  - A. Freehold ownership in severalty of the unit plus an undivided interest in the common elements as a tenant in common
  - B. Leasehold possession of the unit plus severalty ownership of the common elements
  - C. Freehold ownership of the unit in severalty plus an undivided interest in the common elements as a joint tenant
  - D. Shared ownership with all other unit owners as tenants in common
18. Which of the following could NOT own a property in severalty?
  - A. A general or limited partnership
  - B. Co-owners
  - C. An individual
  - D. A corporation, LLC, or trust
19. Which of the following condominium features would be considered a limited common element?
  - A. Driveways leading to the garage
  - B. Walking paths leading to the unit
  - C. Trees viewable from the unit
  - D. Reserved parking space

# UNIT 4 BROKER-LEVEL QUESTIONS

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1. A form of co-ownership with no rights of survivorship is known as
  - A. tenancy by the entirety.
  - B. community property.
  - C. dower and curtesy.
  - D. tenancy in common.
2. Two doctors were co-owners in fee simple of a small office building. One of the doctors died intestate and left nothing to be distributed to heirs. The surviving owner is neither related to the deceased nor the deceased's creditor. How did the surviving owner acquire the deceased owner's interest in the office building?
  - A. Joint tenancy
  - B. Reversionary rights
  - C. Adverse possession
  - D. Remainder interest

# UNIT 4 QUIZ ANSWERS

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1. **D** The answer is ownership by one person or entity. Severalty refers to sole (severed) ownership.
2. **D** The answer is each tenant owns an undivided interest in the property. While shares in a tenancy in common may be unequal, each co-owner owns his share as an indivisible percentage of the entire property.
3. **A** The answer is tenancy in common. In a tenancy in common, the deceased person's interest goes to the decedent's heirs or other devisees named in the will. There is no right of survivorship.
4. **A** The answer is joint tenants. Multiple ownership with the right of survivorship to co-owners is joint tenancy.
5. **D** The answer is to develop and construct new units. Owners associations manage the condominium complex, but they do not develop or construct units.
6. **A** The answer is a condominium. In a condominium, the owner owns and finances an individual unit. In a cooperative, the owner finances the shares of stock that represent ownership in the cooperative, and has a proprietary lease providing rights of possession to the unit.
7. **D** The answer is limited to the amount of the limited partner's investment in the partnership. A limited partner's liability is limited to the amount of the limited partner's investment in the partnership.
8. **D** The answer is all current owners as tenants in common. Common elements are owned by all unit owners as tenants in common.
9. **D** The answer is describe the choices and, if the couple is still undecided, recommend they speak to an attorney or a financial planner. Typically, the salesperson is allowed to describe each type of co-ownership tenancy but may not recommend how to take title. The salesperson should recommend that the buyer seek expert counsel of an attorney or a financial planner.
10. **D** The answer is a time-share. A time-share is the right to possess a property for a predetermined amount of time.
11. **A** The answer is resort and vacation properties. The vast majority of time-shares are sold at resorts and vacation spots around the world.
12. **B** The answer is a deed. Cooperative owners do not own any real estate; therefore, they never receive a deed. The proprietary lease and share of stock are personal property.
13. **C** The answer is attend the annual homeowners association meeting. Not attending when a vote is taking place, however, or not voting by proxy, is often counted as a yes or no vote.
14. **A** The answer is single-family home subdivision. The typical subdivision creates single-family lots and homes.
15. **D** The answer is all of these. Common elements are owned by all owners as tenants in common, and are available for use by condominium owners. Association dues are used to pay for the upkeep and maintenance of the common elements.
16. **C** The answer is limited common elements. Limited common elements are owned by all the unit owners as tenants in common, but are reserved for use by one unit owner.

17. **A** The answer is freehold ownership in severalty of the unit plus an undivided interest in the common elements as a tenant in common. The condominium owner owns the unit plus a percentage of all common elements. This is considered a single parcel for property tax purposes.
18. **B** The answer is co-owners. Ownership in severalty means there is one single owner. The owner may be a person or an entity—there is one name on the deed. Co-ownership means there is more than one owner.
19. **D** The answer is reserved parking garage. Limited common elements are owned by all unit owners, but are reserved for exclusive use by one unit owner.

### Broker-Level Questions

1. **D** The answer is tenancy in common. Co-owners in tenancy in common have no rights of survivorship. Tenancy by the entirety and community property are similar to joint tenancy for married couples only. Dower and curtesy are laws on the distribution of a deceased person's property that are used in some states.
2. **A** The answer is joint tenancy. Upon the death of an owner in a joint tenancy, all remaining interests pass to the surviving co-owner(s) via the right of survivorship.



# UNIT 5

## Land Description

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Identify the methods used for describing real estate.
- › Explain the process involved in identifying and measuring property rights including those above and below the surface.

### KEY POINTS—UNIT 5

- There are three major types of legal descriptions: metes and bounds, rectangular (government) survey, and lot and block (recorded plat).
- The metes-and-bounds method describes land by a series of courses (compass directions) and distances. It starts at a defined “point of beginning” (POB), then describes the boundaries of the parcel until an enclosed tract of land has been described.
- The rectangular (government) survey describes land by reference to a series of grids. A series of ranges, tiers, and townships relative to a principal meridian and a baseline are used to locate the property.
- The lot-and-block (recorded plat) method describes land by referring to a lot number on a plat map that has been filed and recorded with the county recorder. Because the plat map contains a detailed description of the land, simple reference to the plat map is sufficient. This method is also called the lot-and-block method or the subdivision plat method.
- A survey or an improvement location certificate (ILC) may be used to establish and find property boundaries. Both documents will also identify encroachments.
- A valid deed must contain a legal description of the land being conveyed.

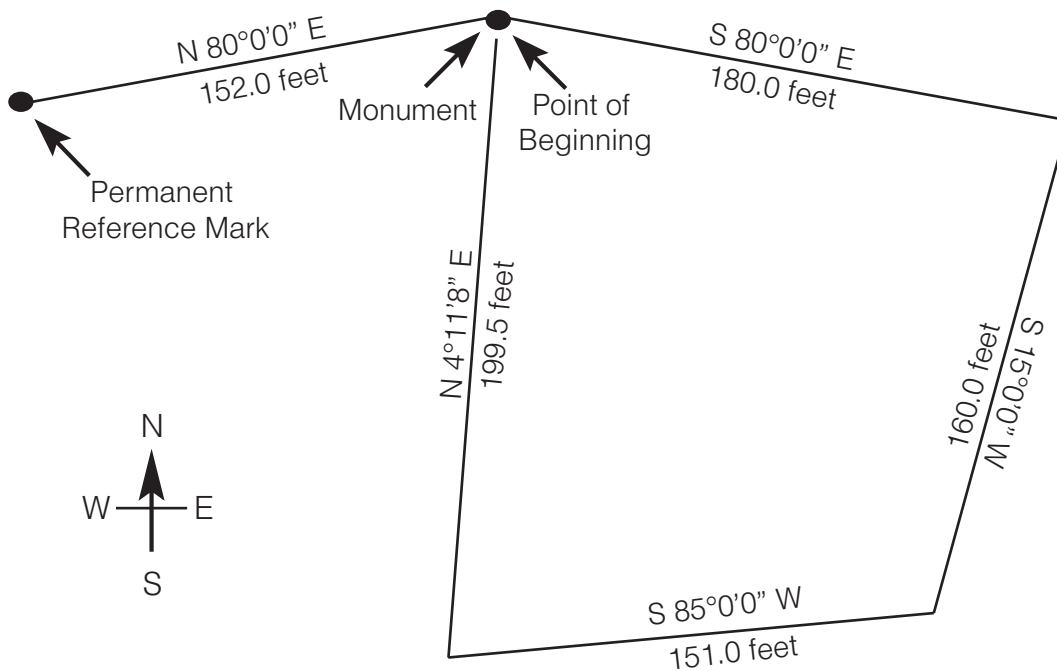
## I. METHODS OF DESCRIBING REAL ESTATE

### A. Most common methods

1. The three most common are metes and bounds, rectangular (government) survey, and lot and block (recorded plat).
2. Legal descriptions describe only the land.
3. The description of the land must be legally sufficient. Street addresses are informal descriptions subject to change, though some states allow a street address to be used in a real estate contract.
4. Some states recognize and permit the use of a Torrens certificate to identify a parcel of real estate.

### B. Metes-and-bounds method (see Figure 5.1)

**Figure 5.1: Metes and Bounds**



Commencing at the permanent reference mark at the Southwest corner of Section 15, thence North 80°0'0" East 152.0 feet to the point of beginning of the property described herein. Thence South 80°0'0" East 180.0 feet; thence South 15°0'0" West 160.0 feet; thence South 85°0'0" West 151.0 feet; thence North 4°11'8" East 199.5 feet to the point of beginning.

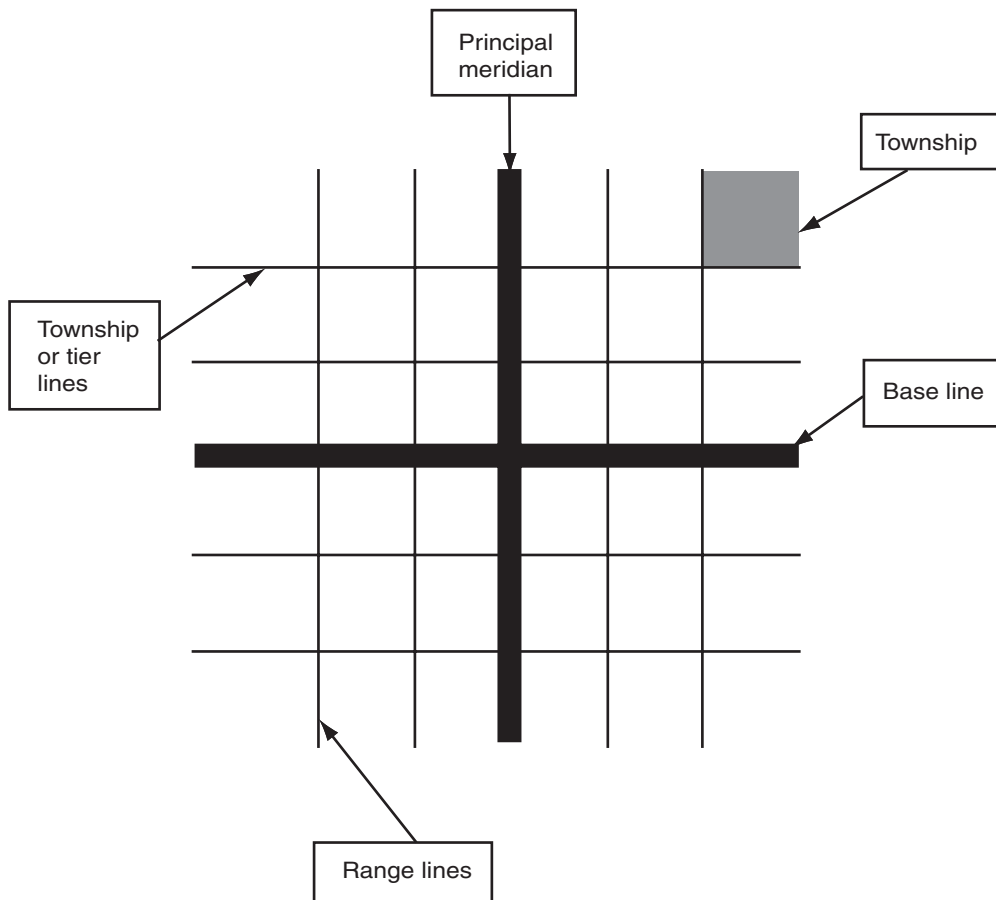
1. Metes: \_\_\_\_\_
2. Bounds: \_\_\_\_\_



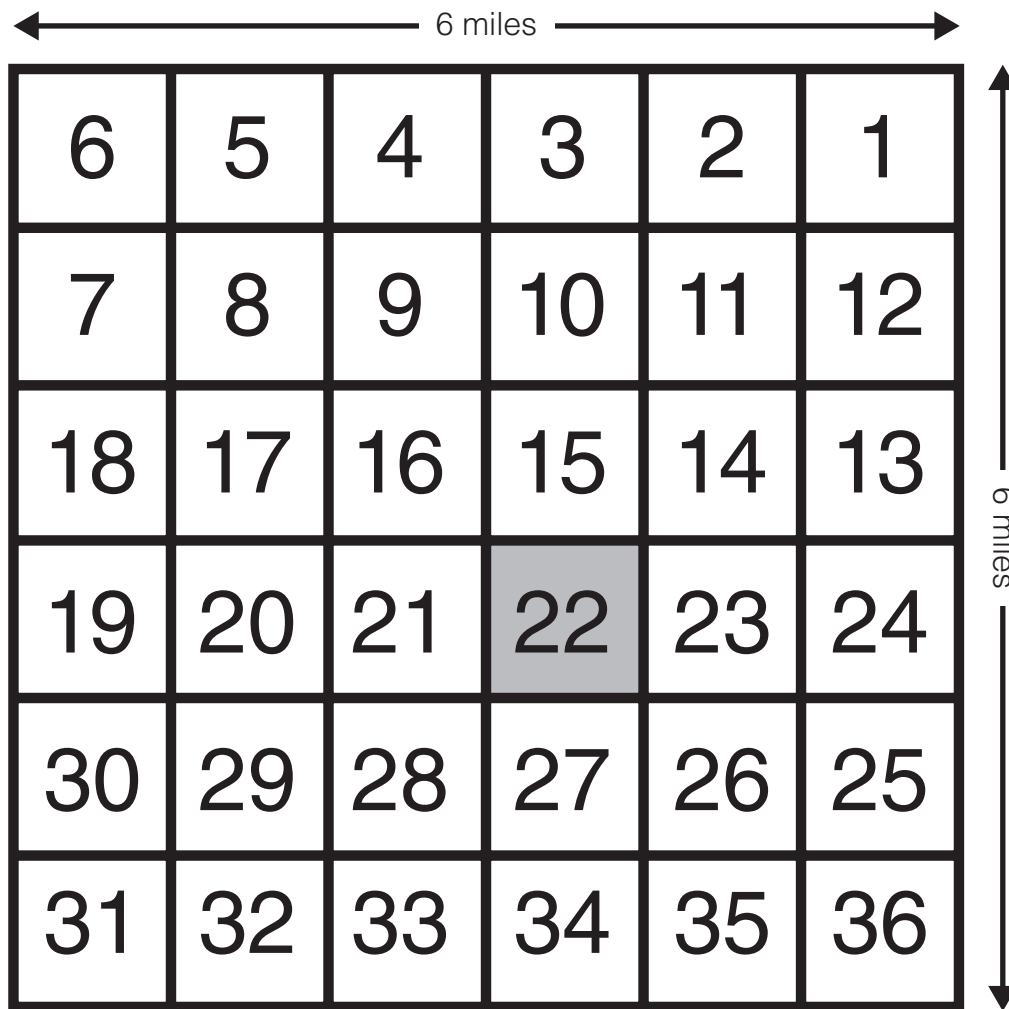
3. Begins and ends at the \_\_\_\_\_
  - a. It is the only description that uses \_\_\_\_\_ and moves in a set direction.
  - b. The description must completely encircle the property.
  - c. Measure in the clockwise direction

**C. Rectangular (government) survey system (see Figure 5.2)**

**Figure 5.2: Rectangular Survey Grid**



1. A rectangular (government) survey is a system developed by the U.S. government that locates a parcel of land within a grid system, based on its location with reference to meridians and range lines that run north-south and baselines and township (tier) lines that run east-west.
2. There are 37 principal meridians in the United States, and each is referenced by a name or meridian number.
3. A township is a square that is six miles by six miles, bounded by the specified ranges and tiers (see Figure 5.3).

**Figure 5.3: Section 22, Township 3 North, Range 3 East of the Sixth Principal Meridian**

4. A \_\_\_\_\_ is a vertical row of townships (north-south).
5. A \_\_\_\_\_ is a horizontal row of townships (east-west).
6. Each township contains 36 sections.
7. A section is one mile by one mile square and contains \_\_\_\_\_.
8. An acre contains \_\_\_\_\_ square feet.

#### **D. Determining the price of parcels**

1. The N  $\frac{1}{2}$  of the SW  $\frac{1}{4}$  of the NE  $\frac{1}{4}$  of the SE  $\frac{1}{4}$  sold for \$8,500 per acre. What was the selling price?

A section has \_\_\_\_\_ acres.

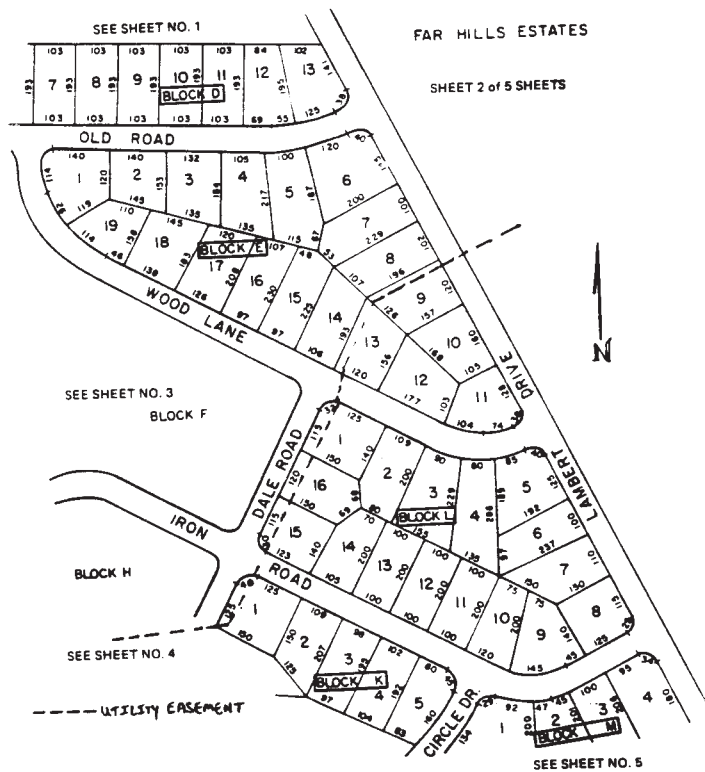
Divide 640 acres by the denominators in the description (the denominator of  $\frac{1}{2} = 2$ , the denominator of  $\frac{1}{4} = 4$ , etc.). The denominators in this example are 2, 4, 4, 4.

$640 \text{ acres} \div 2 \div 4 \div 4 \div 4 = \underline{\hspace{2cm}}$

2.  $5 \text{ acres} \times \$8,500 \text{ per acre} = \underline{\hspace{2cm}}$  selling price

### E. Recorded plat map (see Figure 5.4)

Figure 5.4: Plat Map



1. The lot-and-block method is also called the recorded plat method.
2. A subdivision plat is a \_\_\_\_\_ that is created by engineers and surveyors to show streets and the location and boundaries of individual lots in a subdivision.
3. When approved by building officials, \_\_\_\_\_ in the county recorder's office in the county where the property is located.
  - a. No lot sales or construction may occur until the plat is recorded.
4. This system is most common in \_\_\_\_\_ areas.
5. Recording a subdivision plat is a common way for streets in developments to be dedicated for public use.

## II. THE SURVEY: MEASURING PROPERTY RIGHTS

### A. Legal descriptions

1. A survey is used to \_\_\_\_\_.
  - a. A \_\_\_\_\_ is an onsite measurement of property lines and the location of houses, easements, and encroachments.
  - b. Elevation is measured from a \_\_\_\_\_.
  - c. The survey uses monuments, which are visible markers that establish \_\_\_\_\_.
  - d. \_\_\_\_\_ are monuments that serve as permanent reference points throughout the United States.
2. An improvement location certificate (ILC) or mortgage survey locates improvements on the property but is not used to legally establish property boundaries.
  - a. Either will reveal \_\_\_\_\_ and zoning violations, such as setback requirements.

### B. Land units and measurements

1. A \_\_\_\_\_ is 5,280 feet.
2. A square mile is \_\_\_\_\_.
3. An acre is \_\_\_\_\_.
4. By tradition, the dimensions of a building lot indicate the frontage first.
  - a. Width = street frontage
  - b. Length = depth of the lot (the distance from the front property line to the rear property line)
  - c. Example: A lot 57 feet wide by 108 feet deep
    - i. is described as 57 ft  $\times$  108 ft, or simply 57  $\times$  108; and
    - ii. has 57 feet street frontage and is 108 feet deep.
5. The area of a lot is calculated as follows: width  $\times$  length = area ( $W \times L = A$ ).

## UNIT 5 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

640	monuments	street frontage
43,560	point of beginning	survey
clockwise	recorded	townships
frontage	rectangular (government)	
lot, block, and subdivision	survey	
metes and bounds	sections	

1. Townships, sections, and meridians are used in the \_\_\_\_\_ form of legal description.
2. A legal description that uses compass degrees and measurements is \_\_\_\_\_.
3. The type of legal description most common in urban areas is \_\_\_\_\_.
4. The rectangular survey grid system divides land into \_\_\_\_\_, each being a six-mile-by-six-mile square.
5. Each township is divided into 36 \_\_\_\_\_ that each measure one mile by one mile.
6. A section contains \_\_\_\_\_ acres.
7. An acre contains \_\_\_\_\_ square feet of land.
8. Surveyors use permanent visible reference points known as \_\_\_\_\_ to establish property boundaries.
9. The best way for a property owner to establish boundaries and identify encroachments is to have a(n) \_\_\_\_\_ completed.
10. A metes-and-bounds legal description begins and ends at a(n) \_\_\_\_\_, describing compass readings and measurements in a(n) \_\_\_\_\_ direction.
11. In practice, rectangular lot measurements usually are given stating the \_\_\_\_\_ measurement, or width, first, followed by the length or depth of the lot.
12. Lots in a subdivision development cannot be sold until the developer's plat map is \_\_\_\_\_.

## UNIT 5 GLOSSARY REVIEW ANSWERS

1. rectangular (government) survey
2. metes and bounds
3. lot, block, and subdivision
4. townships
5. sections
6. 640
7. 43,560
8. monuments
9. survey
10. point of beginning, clockwise
11. frontage
12. recorded

# UNIT 5 QUIZ

---

1. Section 4 contains how many acres?
  - A. 40 acres
  - B. 160 acres
  - C. 640 acres
  - D. 43,560 acres
2. A survey would do all of the following EXCEPT
  - A. establish boundaries.
  - B. create legal descriptions for plat maps.
  - C. reveal an illegal use, such as a commercial use in a residential zone.
  - D. find encroachments.
3. Real estate is bought and sold based on
  - A. street addresses.
  - B. property descriptions.
  - C. plat sizes only.
  - D. plats and parcels.
4. A developer bought a 100-acre parcel to subdivide into 1-acre home sites. Which of the following methods of legal description would BEST achieve the developer's objectives?
  - A. Rectangular survey
  - B. Monuments
  - C. Lot and block
  - D. Metes and bounds
5. The N  $\frac{1}{2}$  of the SW  $\frac{1}{4}$  of the NE  $\frac{1}{4}$  of the S  $\frac{1}{2}$  sold for \$1,000 per acre. What was the selling price?
  - A. \$1,000
  - B. \$5,000
  - C. \$8,000
  - D. \$10,000
6. The method of legal description that uses townships and meridians is called
  - A. a rectangular survey.
  - B. metes and bounds.
  - C. an informal reference.
  - D. a street address.
7. After completing the plat map, the developer's next step is to
  - A. request a certificate of occupancy.
  - B. pull the building permits.
  - C. record the plat map.
  - D. sell the lots.
8. Which legal description uses compass degrees and measurements?
  - A. Metes and bounds
  - B. Rectangular survey
  - C. Lot and block
  - D. Recorded plat
9. Which method of legal description uses plat maps?
  - A. Informal description by street address or rural route
  - B. Lot and block
  - C. Rectangular survey
  - D. Metes and bounds
10. The legal description of land that uses meridians and sections is
  - A. rectangular survey.
  - B. metes and bounds.
  - C. lot and block.
  - D. township.
11. A method of property description that uses monuments, a point of beginning, and describes the boundaries of a property in a clockwise direction is
  - A. the lot and block method.
  - B. the metes-and-bounds method.
  - C. the rectangular survey method.
  - D. the maps and plats method.

12. Which of the following BEST defines a plat?
  - A. A method of legal description using sections, townships, and ranges
  - B. An informal reference to properties in a neighborhood
  - C. A document used to record the streets and lots in a subdivision of land
  - D. An instrument used by surveyors to locate property boundaries
13. Which of the following is NOT considered a legal description?
  - A. Street address
  - B. Metes and bounds
  - C. Government survey
  - D. Recorded plat
14. A residential lot measures 50 ft.  $\times$  200 ft. Approximately what part of an acre is the property?
  - A. Eighth
  - B. Quarter
  - C. Third
  - D. Half



# UNIT 5 BROKER-LEVEL QUESTIONS

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1. The main purpose of legal descriptions is to
  - A. provide a backup for the street address, which is the preferred description.
  - B. create an easily recognizable property locator.
  - C. describe the exact location of real property based on known surveyed boundaries.
  - D. provide the buyer with a complete list of all real and personal property being conveyed in the deed.

# UNIT 5 QUIZ ANSWERS

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1. **C** The answer is 640 acres. A section contains 640 acres.
2. **C** The answer is reveal an illegal use, such as a commercial use in a residential zone. A survey would not find an illegal use.
3. **B** The answer is property descriptions. Real estate is bought and sold based on property descriptions (also called legal descriptions).
4. **C** The answer is lot and block. A subdivided (recorded) plat is the simplest way to divide a large parcel into smaller lots.
5. **D** The answer is \$10,000. A section contains 640 acres. Divide by the denominators in the legal description to determine the acreage:  $640 \div 2 \div 4 \div 4 \div 2 = 10$  acres;  $10 \text{ acres} \times \$1,000 \text{ per acre} = \$10,000$ .
6. **A** The answer is a rectangular survey. The government survey (rectangular survey) established sections, townships, and ranges in the western United States.
7. **C** The answer is record the plat map. After receiving the plat map, the second step is to record the map. Then, the lots can be sold and building permits can be issued.
8. **A** The answer is metes and bounds. Metes-and-bounds descriptions start at a point of beginning and are described in a clockwise direction leading back to the point of beginning.
9. **B** The answer is lot and block. The lot-and-block (recorded plat) method of description uses plat maps to show the location and boundaries of individual lots in a land subdivision.
10. **A** The answer is rectangular survey. The rectangular survey uses meridians, baselines, townships, and sections to describe land.
11. **B** The answer is the metes-and-bounds method. The metes-and-bounds method of legal description uses distance and direction measurements to describe the boundaries of a property.
12. **C** The answer is a document used to record the streets and lots in a subdivision of land. A plat is a map showing the location and boundaries in a subdivision.
13. **A** The answer is street address. Street addresses are informal descriptions and are not considered legal descriptions. Some states allow street addresses to be used in real estate contracts, but a deed must contain a legal description.
14. **B** The answer is quarter.  $50 \text{ ft.} \times 200 \text{ ft.} = 10,000 \text{ sq. ft.}$ , which is approximately one-quarter of the 43,560 sq. ft. in an acre.

## Broker-Level Questions

1. **C** The answer is describe the exact location of real property based on known surveyed boundaries. Legal descriptions describe the exact location of real property based on known surveyed boundaries. Because legal descriptions are created through surveys of large tracks of land, a survey is the best reference for real property.

# UNIT 6

## Transfer of Title

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the fundamental concepts of title as it relates to the ownership of land, and the processes and instruments used to apply these concepts.
- › Describe the circumstances and conditions that may provide for the involuntary transfer of title.
- › Explain testate, intestate, wills, and the probate process.

### KEY POINTS—UNIT 6

- Title refers to the right to or ownership of real property.
- A deed is the document used to transfer title to real property. A valid deed must identify the parties, have a competent grantor, contain words of conveyance, contain a legal description of the property, state that consideration was given, be properly executed, and be delivered and accepted. The statute of frauds requires that the deed be in writing.
- The three main types of deeds used are the general warranty deed, special warranty deed, and quitclaim deed.
- A general warranty deed carries five basic covenants: seisin, quiet enjoyment, against encumbrances, further assurance, and warranty forever. This deed provides the greatest protection for a grantee (typically the buyer who is receiving title to real property).
- A special or limited warranty deed warrants title only for the time the grantor owned the real estate. Unlike a general warranty deed, it does not give any warranties for past or future claims unless the claim is for the period the grantor owned the property.
- A quitclaim deed conveys no warranties of any kind. It simply conveys whatever interest the grantor has when the deed is delivered. A quitclaim deed may be used as a “problem solver” to clear clouds on the title.
- When a person dies, the person’s property may be transferred by the terms of a will or according to the state’s rules of descent, which govern intestate succession.

- Property may also be acquired by adverse possession. The adverse possession must be open, continuous, exclusive, actual, and notorious (hostile) for a period of years that are determined by each state.

## I. REMEMBERING LEGAL TERMINOLOGY

**Figure 6.1: “ORs” and “EEs” Table**

Document	ORs Give	EEs Receive
Deed	Grant _____	Grant _____
Lease	Less _____	Less _____
Mortgage	Mortgag _____ (borrower)	Mortgag _____ (lender)
Offered contract	Offeror	Offeree
Accepted contract	Vendor	Vendee
Loan	M _____ tgag _____ (b _____ rr _____ wer)	Mortgag _____ (l _____ nd _____ r)
Deed	Grantor	Grantee
Lease	Lessor	Lessee
Option contract	Optionor	Optionee

## II. CONVEYING OWNERSHIP

### A. Act of conveying ownership (transferring title) of real estate from one party to another is the process called \_\_\_\_\_

1. A \_\_\_\_\_ is the document that transfers title from grantor to grantee during the grantor's lifetime.
2. A deed is \_\_\_\_\_ by the grantor.
3. The \_\_\_\_\_ is the recipient of the deed.

### B. Voluntary alienation

1. Voluntary alienation is the transfer of title during the property owner's lifetime by the document called a \_\_\_\_\_.
2. The purpose of a deed is the voluntary transfer of title between the grantor and the grantee.
3. A seller of real property is required to provide \_\_\_\_\_.
4. Every deed conveys whatever interest is held by the grantor, unless it specifically states it is conveying a lesser interest, such as when the seller withholds mineral rights.
5. The major difference between types of deeds is the extent of the promises given by the grantor to the grantee.
6. Deeds do not \_\_\_\_\_, though recorded deeds provide very strong evidence of ownership.
7. Deeds do not have to be recorded for title to transfer; title passes upon acceptance by the grantee.

**C. Requirements for a valid deed (see Figure 6.2)**

1. A competent grantor
  - a. \_\_\_\_\_
  - b. The seller is the \_\_\_\_\_ and the buyer is the \_\_\_\_\_.
2. Execution by the grantor(s)
  - a. The deed must be signed by all owners to convey the property.
  - b. An \_\_\_\_\_ is a formal declaration under oath that the person who signs a written document does so voluntarily and that the signature is genuine.
  - c. A corporation can convey real estate if authorized by its bylaws and the deed must be signed by an authorized officer of the corporation.
3. An identifiable grantee
4. A legal description of the land (property description)
  - a. Legal descriptions \_\_\_\_\_. Appurtenances are presumed to transfer with the land unless specifically excluded.
5. Consideration
  - a. Money or \_\_\_\_\_
  - b. “One dollar and other good and valuable consideration”
6. Words of conveyance (granting clause)
  - a. State that the seller is making a grant that conveys or transfers the warranties of the deed
  - b. The habendum clause defines the type of freehold estate being granted.
    - i. For example: “To have and hold forever” conveys fee simple absolute ownership.
7. Delivery to and acceptance by the grantee(s)
  - a. Title passes upon \_\_\_\_\_.
  - b. The grantee has the right to refuse the deed.

**Figure 6.2: Requirements for a Valid Deed**

- 
1. Competent grantor
  2. Identifiable grantee
  3. Words of conveyance
  4. Legal description
  5. Consideration
  6. Execution by grantor
  7. Delivery and acceptance (by grantee)
- 

**D. Types of conveyance deeds**

1. General warranty deed
  - a. Includes the \_\_\_\_\_
  - b. Greatest protection for the \_\_\_\_\_
  - c. Contains five covenants and warranties of title
    - i. Covenant of \_\_\_\_\_: grantor owns and has right to convey
    - ii. Covenant against encumbrances: no undisclosed encumbrances (liens, restrictions, easements)
    - iii. Covenant of further assurances: future cooperation in signing additional documents
    - iv. Covenant of \_\_\_\_\_: grantee will not be disturbed by others claiming title to the property
    - v. \_\_\_\_\_: guarantee of defense of title against claims such as liens or easements
2. Special (limited) warranty deed
  - a. Grantor only warrants title against defects that may have arisen during \_\_\_\_\_, not those of earlier property owners.
  - b. No warranties against \_\_\_\_\_
3. \_\_\_\_\_
  - a. Least liability for the \_\_\_\_\_
  - b. No covenants or warranties—"If I have an interest, I transfer that interest to you."
  - c. Used to clear clouds on title (problem solver)
  - d. Would use when grantor wants no future claims or \_\_\_\_\_

#### 4. Other deeds

- a. A bargain and sale deed does not warrant against liens or encumbrances but warrants the grantor's right to convey title.
- b. Personal representative/probate deed
- c. A trustee's deed/sheriff's deed/certificate of sale transfers title at the end of a foreclosure proceeding or statutory redemption period.
- d. A reconveyance deed is used when the borrower pays off a loan secured by a deed of trust.
- e. A deed of trust is the security instrument used in some states by which a borrower (trustor) conveys legal title to a third party (trustee) for the benefit of the lender (beneficiary).

#### E. Transfer tax stamps

1. Most states impose a state transfer tax on conveyances of real estate.
2. The \_\_\_\_\_ may be paid by either the seller or the buyer, or split between them.

### III. INVOLUNTARY ALIENATION

#### A. Adverse possession

1. Ownership recognized by the courts after open, \_\_\_\_\_, continuous, hostile, and adverse \_\_\_\_\_ of another's land for a certain period set by state law

#### B. Easement by prescription/prescriptive easement

1. Easement recognized by the courts after open, continuous, exclusive, actual, and notorious (hostile) \_\_\_\_\_ of another's land for a certain period set by state law
  - a. Possession or use must be open (visible), continuous, exclusive (distinct), actual, and notorious (hostile—without permission) (OCEAN).

#### C. Key points

1. The law presumes owners of real property will regularly inspect their property and protect their interest by giving a notice to cease and desist to anyone who is trespassing.
2. Owners who do not inspect their property may lose their rights of ownership if another party possesses or uses the property for a statutory period of time.
3. Title obtained by adverse possession or an easement by prescription is not voluntarily granted by the property owner but is granted through a court procedure.
4. Owners who are aware of possession and use by another and have given the possessing/using party permission (license) do not fall under this law.
5. If all parties know and agree to the possession or use, it cannot be adverse possession or easement by prescription.

#### IV. CONVEYANCE OF A DECEDENT'S PROPERTY

##### A. Transfer by will (testate)

1. Testator is the person who makes \_\_\_\_\_.
2. A deceased person's interest in real property is transferred to another by a \_\_\_\_\_.
3. Bequest is the act of transferring a deceased person's interest in \_\_\_\_\_.
4. The advantage of a will is that all heirs are known and there is no chance of \_\_\_\_\_.

##### B. Intestate succession— \_\_\_\_\_

1. Heirs/descendants are determined by state laws of descent.
2. If there are no heirs, the property will escheat to the state.

##### C. Probate

1. Probate is the process of distributing all of a deceased person's assets.
2. \_\_\_\_\_ in order for the devisee to receive real property.



## UNIT 6 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

adverse possession	grantee	quiet enjoyment
deed	grantor	quitclaim deed
delivered and accepted	notarized	special warranty deed
easement by prescription	possession	testator
general warranty	probate	use

1. A written legal document by which ownership of real property is transferred from one party to another is a(n) \_\_\_\_\_.
2. The two parties to a deed are the owner/\_\_\_\_\_ and the recipient/\_\_\_\_\_.
3. To convey title, the deed must be signed by the \_\_\_\_\_.
4. Title does not pass to the grantee until the deed is \_\_\_\_\_.
5. Assurance to grantees that they will not be disturbed by someone else with a lawful ownership interest in the property is the covenant of \_\_\_\_\_.
6. The type of deed that is considered the best deed for a grantee is a(n) \_\_\_\_\_.
7. A deed that conveys whatever interest in the property the grantor holds at the time of conveyance, has no liability for the grantor, and contains no covenants or warranties is a(n) \_\_\_\_\_.
8. A deed that warrants only against title defects that arose during the period the grantor owned the property is a(n) \_\_\_\_\_.
9. Most deeds must be \_\_\_\_\_ to be recorded.
10. A(n) \_\_\_\_\_ is a person who has written a last will and testament.
11. An example of involuntary alienation, \_\_\_\_\_ is ownership recognized by the courts after open, notorious, continuous, hostile, and adverse \_\_\_\_\_ of another's land for a statutory period of time.
12. A court of law may grant a trespasser a(n) \_\_\_\_\_ after open, continuous, exclusive, actual, and notorious (hostile) \_\_\_\_\_ of another's land for a period of time determined by state law.
13. The process of honoring a will by distributing a deceased person's assets is known as \_\_\_\_\_, a legal process that is overseen by the courts.

## UNIT 6 GLOSSARY REVIEW ANSWERS

1. deed
2. grantor, grantee
3. grantor
4. delivered and accepted
5. quiet enjoyment
6. general warranty deed
7. quitclaim deed
8. special warranty deed
9. notarized
10. testator
11. adverse possession, possession
12. easement by prescription, use
13. probate

# UNIT 6 QUIZ

---

1. In a quitclaim deed, the grantor covenants
  - A. that the title is marketable.
  - B. nothing and has no future liability.
  - C. that the grantor owns the property and has the right to convey title.
  - D. that the grantor will defend any claims against the title.
2. To be valid, a deed must have
  - A. a property description.
  - B. a list of encumbrances.
  - C. a competent grantee.
  - D. a description of all improvements.
3. Regarding a deed, *execution* refers to
  - A. notarization.
  - B. recordation.
  - C. delivery and acceptance.
  - D. the signature(s) of the grantor(s).
4. The covenant affirming that the grantor holds title and has the right to convey it to another is the covenant
  - A. of further assurance.
  - B. against encumbrances.
  - C. of quiet enjoyment.
  - D. of seisin.
5. If a lender wanted to convey title on a foreclosed property with no warranties to the grantee and no liabilities to the grantor, it would be logical to use
  - A. a quitclaim deed.
  - B. a special warranty deed.
  - C. a warranty deed.
  - D. a sheriff's deed.
6. The probate process
  - A. settles disputes between co-owners of property.
  - B. rules on warranty claims.
  - C. is required if the party died testate.
  - D. determines claims under adverse possession.
7. Which parties must sign a deed to make it valid?
  - A. Grantors only
  - B. Grantees only
  - C. Both grantors and grantees
  - D. Lessees only
8. Which of the following gives the grantee the MOST protection?
  - A. General warranty deed
  - B. Limited warranty deed
  - C. Quitclaim deed
  - D. Bargain and sale deed
9. Which of the following is NOT essential to the validity of a deed?
  - A. Recording
  - B. Competent grantor
  - C. Execution by the grantor
  - D. Words of conveyance
10. All of the following are advantages of having a will EXCEPT
  - A. all heirs are known.
  - B. there is no possibility of the real property escheating to the government.
  - C. the testator is known and controls what will be in the will.
  - D. state laws of descent, which are less strict, will apply.
11. Conveyance of title occurs at the moment
  - A. the deed is delivered and accepted.
  - B. the deed is recorded.
  - C. the grantor receives the consideration.
  - D. the deed is signed by the grantor.
12. The deed that limits the grantor's warranties to the grantor's period of ownership is
  - A. the quitclaim deed.
  - B. the special warranty deed.
  - C. the general warranty deed.
  - D. the trustee's deed.
13. A right acquired by a nonowner through open and notorious use of the land of another is an easement
  - A. by expression.
  - B. appurtenant.
  - C. by prescription.
  - D. by necessity.

14. A party that takes possession of another's real property without permission may, in the future, be able to claim
  - A. title due to adverse possession.
  - B. prescriptive easement rights.
  - C. a qualified fee estate.
  - D. reversionary rights.
15. All of the following are necessary for a valid deed EXCEPT
  - A. the signature of the grantee.
  - B. words of conveyance.
  - C. a legal description.
  - D. the names of the parties.
16. Which is MOST closely associated with the voluntary alienation of real property?
  - A. Bill of sale
  - B. Adverse possession
  - C. Deed
  - D. Easement by prescription
17. The person who signs the deed and conveys title is called
  - A. the trustor.
  - B. the lessor.
  - C. the grantee.
  - D. the grantor.
18. An owner of a ranch has become reclusive and has not left his home for 30 years. On the far side of the ranch, his neighbor built a barn and corral 25 years ago. In this situation, the neighbor
  - A. will lose all the improvements and land if the owner gives notice.
  - B. has stolen real property and may go to prison.
  - C. may try to claim title through adverse possession and a suit to quiet title.
  - D. will have the right to sell the improvements to the ranch owner because no notice was given.
19. A property was sold by a married couple using a general warranty deed. After closing, the buyer discovered there was a third owner who had not signed the deed. The sellers broke the covenant of
  - A. quiet enjoyment.
  - B. further assurances.
  - C. seisin.
  - D. warranty forever.

# UNIT 6 BROKER-LEVEL QUESTIONS

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1. All of the following are true of a will EXCEPT
  - A. if the real property is owned in joint tenancy, the will does not need to go through probate.
  - B. probate is required for all wills, even those only distributing personal property.
  - C. the testator can change the will at any time until death.
  - D. the heirs receive a bequest or devise.
2. On the deed, the broker has verified the competency and signature of the grantor, the legal description, and the delivery and acceptance by the named grantee. What are the other items needed to make a valid deed?
  - A. Signed and recorded
  - B. Words of conveyance and consideration
  - C. Delivery, execution, and recordation
  - D. Identifiable grantor and consideration
3. During a property inspection, an out-of-town owner noticed that a shed and garden had been built on the property. A neighbor working in the garden told the owner she intends to take title to the property through adverse possession. The owner gave the gardener written permission to continue using the property for the shed and garden. Will the gardener be able to obtain title in the future?
  - A. Yes, if the gardener meets the requirements of time for adverse possession
  - B. No; the owner has given notice, so the gardener will have an easement by prescription
  - C. Yes, but since the gardener received notice, there will be additional requirements to take title
  - D. No; the gardener has been given a license, and the owner may revoke permission to possess or use the property at any time

# UNIT 6 QUIZ ANSWERS

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1. **B** The answer is nothing and has no future liability. There are no covenants (promises) in a quitclaim deed.
2. **A** The answer is a property description. Valid deeds must contain a property (or legal) description.
3. **D** The answer is the signature(s) of the grantor(s). The grantor signs the deed to convey his ownership interest to the grantee named in the deed.
4. **D** The answer is of seisin. The covenant of seisin affirms that the grantor owns and has the right to convey title.
5. **A** The answer is a quitclaim deed. A quitclaim deed conveys whatever title the grantor holds and gives no warranties or covenants, past or future. This deed would allow the bank to have no future title claims or liabilities.
6. **C** The answer is required if the party died testate. Probate is the process by which a deceased person's instructions are carried out and is required if the party died testate (with a will).
7. **A** The answer is grantors only. A deed is an instrument to transfer title, not a contract. The grantors sign (execute) the deed, transferring their interest to the grantee. The grantors sign (execute) the deed.
8. **A** The answer is general warranty deed. The general warranty deed, in which the grantor gives five covenants and warranties, offers the grantee the most protection.
9. **A** The answer is recording. While deeds should always be recorded, deeds do not have to be recorded to be valid.
10. **D** The answer is state laws of descent, which are less strict, will apply. State laws of descent apply to persons who die without a will, or intestate.
11. **A** The answer is the deed is delivered and accepted. Title transfers upon delivery and acceptance of the deed.
12. **B** The answer is the special warranty deed. The covenants in a special (limited) warranty deed relate only to the grantor's period of ownership.
13. **C** The answer is by prescription. A person who uses the land of another for a specific purpose actually, openly, continuously, exclusively, notoriously, and in a hostile manner for the minimum statutory period may be able to go to court to obtain an easement by prescription.
14. **A** The answer is title due to adverse possession. A party who takes possession of another's real property without permission actually, openly, continuously, exclusively, notoriously, and in a hostile manner for the minimum statutory period may be able to go to court and claim title to the property.
15. **A** The answer is the signature of the grantee. The deed is signed by the grantor(s) only.
16. **C** The answer is deed. A deed is an example of voluntary alienation, in which the grantor willingly severs ownership to the property and conveys it to another.
17. **D** The answer is the grantor. The grantor is the only party required to sign the deed.
18. **C** The answer is may try to claim title through adverse possession and a suit to quiet title. If the neighbor has possessed the property for the statutory amount of time required by the state, the neighbor may use a suit to quiet title to try to obtain title to the property.
19. **C** The answer is seisin. The sellers broke the covenant of seisin, which states they had full ownership and could convey the property.

**Broker-Level Questions**

1. **A** The answer is if the real property is owned in joint tenancy, the will does not need to go through probate. Property held as joint tenants does not go through probate, but the will must go through to distribute the other belongings and property owned by the testator.
2. **B** The answer is words of conveyance and consideration. Words of conveyance and consideration are the two missing essential elements. The essential elements are competent grantor; execution by grantor; identifiable grantee who took delivery and acceptance; legal description; consideration; and words of conveyance.
3. **D** The answer is no; the gardener has been given a license, and the owner may revoke permission to possess or use the property at any time. Adverse possession cannot take place if the property owner is aware of the possession or use. By giving the gardener permission, the owner gave the neighbor a license that can be revoked at any time.





# UNIT 7

## Title Records

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain the public recordation system and its importance to the title insurer.
- › Explain the benefits of title insurance and the difference between an owner's policy and a lender's policy.

### KEY POINTS—UNIT 7

- State laws determine how documents are filed for recording. The recording system provides a way of determining who owns a particular piece of real property and the title history of the property.
- Recording a document provides all interested parties with constructive or legal notice of its contents by operation of law. Documents pertaining to a particular parcel are recorded chronologically. Recorded documents are also indexed alphabetically according to the names of the grantor and grantee.
- In many states, the recording system is known as a race-notice system—the first deed to be recorded prevails if that person has received no notice of prior conveyances. State laws determine how documents are filed for recording.
- Marketable title is title that is reasonably free from risk of litigation over possible defects or undisclosed encumbrances.
- The most common way for a seller to demonstrate that the title is marketable is to provide title insurance for the buyer.
- Title insurance companies agree to reimburse the policyholder for losses caused by defects in the title that were not discovered during title search, and will provide legal defense of claims based on covered defects. A title policy insures the owner (the buyer) and/or lender. The purchase contract and tradition determine who pays for the title insurance policy.

- In some states, an abstract with a title opinion is used. The seller updates the abstract, which is a summary of all conveyances, and delivers it to the buyer. The buyer's attorney then renders a title opinion (see Figure 7.1), which states the marketability of the title.

## I. PUBLIC RECORDS

### A. Key points

1. Policies and procedures that regulate recording are established by \_\_\_\_\_.
  - a. These laws also determine who is responsible for organizing and maintaining recorded documents.
2. Recording \_\_\_\_\_ of the document.

### B. Notice and priority

1. Placing a document in the public record provides \_\_\_\_\_
2. The public record establishes \_\_\_\_\_ of interests—first in time, first in right.
  - a. The priority of documents is based on the date and time of recording.
3. A deed does not have to be recorded \_\_\_\_\_.
  - a. A grantee who does not record a deed risks having another party claim title to the property.

### C. Requirements for recording—determined by state law

1. Deeds, mortgages and deeds of trust, contracts for deed, easements, and long-term leases are among the types of documents that are usually recorded.
2. Recorded documents should be executed (signed).
  - a. Most states require documents to be \_\_\_\_\_ (notarized) to be recorded. This confirms that the transfer is voluntary and not under duress.
  - b. A deed that is not recorded lacks \_\_\_\_\_ or legal notice of ownership.
  - c. Creates a cloud on title
3. Recording fee and transfer taxes are determined by state law.
  - a. These include deed tax, documentary fees, tax stamp, mortgage registry tax, and who pays.
  - b. These are typically paid when the deed is recorded.

**D. System allows users to search claims and title**

1. Inspect property for visible claims and \_\_\_\_\_ notice, such as parties in possession or encroachments
2. Inspect public records for \_\_\_\_\_, such as liens and persons on the title
3. Part of buyers' due diligence is to inspect (or have someone inspect) both the property (e.g., home inspection) and public records (e.g., title search).

**E. Title search and abstract of title**

1. A title examiner reviews public records pertaining to a property.
  - a. Identifies ownership, wills, judicial proceedings, and other encumbrances that may affect title
2. The search is from the present to the original source of title.
  - a. The original source may be a land grant or a U.S. patent.
  - b. Many states have adopted the marketable title act.
    - i. Allows title searches to go back for only a certain period of years (e.g., 30 or 60)
3. The process is used to establish the \_\_\_\_\_.
  - a. The chain of title is a history of successive recorded ownership documents linked together.
  - b. The examiner seeks an unbroken chain.
4. Anything that may cast doubt on marketable title is a \_\_\_\_\_.
  - a. Examples: a gap in the chain of title, unreleased lien, undisclosed encumbrances, court orders, etc.
  - b. The seller will need to clear the title to convey marketable title.
  - c. Small issues, such as an unrecorded name change, may be corrected with a correction or quitclaim deed.
  - d. Larger issues may require a lawsuit to quiet title.

**F. Marketable title**

1. Marketable (merchantable) title
  - a. Good or clear title, reasonably free from the risk of litigation over possible defects
  - b. The buyer's goal is to obtain marketable title.
2. Brokers and salespeople must know the requirements to make documents valid, including
  - a. what makes title marketable,
  - b. how ownership issues may impact the transfer of title,
  - c. the essential elements of contracts and deeds, and
  - d. who is required to sign each document in the transaction.

**II. PROOF OF OWNERSHIP****A. Certificate of title**

1. A certificate of title is a \_\_\_\_\_ of all recorded documents affecting title to a given parcel of land, created through a title search.
2. The seller is expected to furnish an updated abstract, which shows all \_\_\_\_\_ recorded interests.
3. The buyer's attorney examines the abstract and traces the chain of title to determine marketability.
4. After tracing the chain of title, the attorney renders a title opinion.
  - a. Shows current status of rights
  - b. \_\_\_\_\_
5. Also called an abstract of title

**B. Attorney's opinion of title**

1. A review of the public records
2. Does not protect against other defects

**Figure 7.1: Sample Title Opinion Letter**

**Wakefield & Lundberg**

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310 Colfax Avenue  
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Generic Real Estate  
823 Ash Street  
Mytown, USA 80000

To whom it may concern:

I have examined the title to the following described premises as the same appears from an abstract of title consisting of 69 entries, which abstract is brought down to date of February 15, 2014, by High Country Abstract Company:

Lot Five (5), Block Three (3), Ridgewood 3rd Addition.

From such examination I am of the opinion that the title to said premises in fee simple is in Gary W. Robinson and Nancy J. Robinson, husband and wife as joint tenants, and that they have a good and marketable title to the same, subject to the rights of any person in possession, to all claims for material or labor furnished within 120 days of the date of certificate, to all questions of surveys, local zoning, and building regulations and subject to the following:

1. Restrictive covenants as shown at entry No. 56 of the abstract.
2. Utility easement as shown at entry No. 56 and revised at entries 63 and 67.
3. A mortgage to City Federal Savings and Loan Association of Minneapolis in the original sum of \$393,850.00 as shown at entry No. 66 of the abstract.
4. Current taxes of \$6,975.73 are one-half paid.

Yours truly,

**Howard S. Wakefield**

Howard S. Wakefield  
HSW:cfh

**C. Title insurance**

1. Best method for insuring marketable title
2. Title search performed by examiner
3. Title insurance company issues a title report and commitment
  - a. The title report
    - i. shows only the \_\_\_\_\_ of ownership and recorded encumbrances, but
    - ii. does not show the \_\_\_\_\_ of past owners or encumbrances.

- b. The commitment lists policy exceptions and recorded defects and encumbrances.
  - i. Exceptions are \_\_\_\_\_ the policy.
    - \_\_\_\_\_: items never covered; buyer responsible for checking
      - Possession, encroachments, unrecorded mechanic's liens, zoning compliance
    - \_\_\_\_\_: clouds specific to the property discovered by examiner
      - Easements, restrictive covenants, current mortgages
- c. The buyer may offer objections before closing.

**D. Types of title insurance policies (see Figure 7.2)**

- 1. Standard \_\_\_\_\_ protects the buyers and their heirs.
  - a. Excludes exceptions/problems listed in the title report
  - b. Cost of coverage is based on the sales price of the property.
  - c. Paid by the seller or the buyer as per the purchase contract
  - d. Coverage continues until the property changes ownership.
  - e. Covers matters of record that are not listed as exceptions, including the following:
    - i. Errors in the title examination
    - ii. Errors in the abstract
    - iii. Errors in the public record, such as misfiled documents
    - iv. Hidden defects, such as forgery, incompetency, misrepresented marital status, and improperly prepared deeds
- 2. An extended owner's coverage policy adds protection against problems that are not a matter of public record but would probably be discovered through inspection (actual notice) of the property, such as the following:
  - a. Parties in possession or adverse possession issues
  - b. Matters of survey, such as encroachments
  - c. Gap period—from title commitment through recording the deed
  - d. Coverage is based on the loan amount.
  - e. Often paid for by the buyer, but the seller could also pay
  - f. Coverage diminishes with each loan payment and ceases to exist when the loan is satisfied.

**Figure 7.2: Title Insurance Coverage**

<b>Not Covered in Any Policy</b>	<b>Standard Coverage—Covered if Found After the Policy Is Issued</b>	<b>Extended Coverage—Covered if Found After the Policy Is Issued</b>
<ul style="list-style-type: none"> <li>■ All exceptions listed in the commitment or policy, including liens</li> <li>■ Defects known to the buyer and the seller</li> <li>■ Zoning use or changes</li> </ul>	<ul style="list-style-type: none"> <li>■ Errors in title examination or the abstract</li> <li>■ Defects found in public records</li> <li>■ Forgery, incompetency, misrepresented marital status, and improperly prepared deeds</li> </ul>	<ul style="list-style-type: none"> <li>■ All items covered in the standard policy, plus               <ul style="list-style-type: none"> <li>– parties in possession,</li> <li>– matters of survey, such as encroachments,</li> <li>– gap period, and</li> <li>– unrecorded liens.</li> </ul> </li> </ul>

**E. The Torrens system**

1. Legal registration system
2. Available in only some states

## UNIT 7 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

abstract of title  
acceptance  
actual  
after  
before  
chain of title  
cloud

constructive  
delivery  
exception  
lis pendens  
marketable title  
notarized  
recording

state laws  
title insurance  
title opinion  
title report  
title search  
valid

1. The priority of a recorded instrument is determined by its date of \_\_\_\_\_.
2. When an attorney or title insurance company traces the ownership of a parcel of land to the beginning of its recorded history, the process is known as a(n) \_\_\_\_\_.
3. A recorded notice stating that a pending lawsuit may affect title to a particular property is a(n) \_\_\_\_\_.
4. A document that summarizes all recorded interests affecting title to a given parcel of land is a(n) \_\_\_\_\_.
5. All the documents that comprise the history of the title are the \_\_\_\_\_.
6. Protection against incomplete or defective records of the title to land can best be obtained by securing \_\_\_\_\_.
7. A defect or problem that is not covered by standard or extended title insurance is a(n) \_\_\_\_\_.
8. Defects in title are covered only if they are found \_\_\_\_\_ closing.
9. A buyer's due diligence includes visually inspecting the property for \_\_\_\_\_ notice and inspecting recorded information in the public record for \_\_\_\_\_ notice.
10. A deed that is not recorded lacks \_\_\_\_\_ notice.
11. The buyer's goal is to obtain \_\_\_\_\_, which is title reasonably free from the risk litigation.
12. After examining the abstract of title on behalf of a buyer, an attorney provides a(n) \_\_\_\_\_.
13. A title insurance company provides a detailed \_\_\_\_\_ showing current title status, along with a commitment to provide title insurance.
14. Anything that casts doubt on marketable title is a(n) \_\_\_\_\_ on title, which the seller may need to clear to deliver good or clear title at closing.



## UNIT 7 GLOSSARY REVIEW ANSWERS

1. recording
2. title search
3. lis pendens
4. abstract of title
5. chain of title
6. title insurance
7. exception
8. after
9. actual, constructive
10. constructive
11. marketable title
12. title opinion
13. title report
14. cloud

# UNIT 7 QUIZ

---

1. A chain of title is
  - A. a form of land measurement used by surveyors on plat maps.
  - B. a form of title insurance resulting in a strong guarantee.
  - C. an encumbrance on title that may prohibit sale of the land.
  - D. a property history of successive conveyances and recorded interests.
2. After sufficient evidence of title is produced, a document that serves as proof of title is issued under the
  - A. abstract of title.
  - B. attorney's title review.
  - C. Torrens system.
  - D. title insurance policy.
3. Which of the following is TRUE about the recording of documents?
  - A. All real estate documents must be recorded to be valid.
  - B. Recording real estate documents provides constructive notice of their contents to the public.
  - C. Recording real estate documents provides actual notice of their contents to the public.
  - D. Recording guarantees a valid and good title.
4. The requirements for recording are determined by
  - A. the county clerk.
  - B. title insurance companies.
  - C. state law.
  - D. federal law.
5. A lender providing a loan secured by a mortgage will MOST likely require the borrower to buy
  - A. a mortgagee's title insurance policy.
  - B. a mortgagor's title insurance policy.
  - C. an owner's title insurance policy.
  - D. private mortgage insurance.
6. Standard coverage title insurance protects against all of the following EXCEPT
  - A. a forged deed.
  - B. encroachments.
  - C. errors in the public record.
  - D. errors in the abstract.
7. A title search examines recorded documents from the current owner to the first recorded source. In doing so, the examiner is tracing or establishing
  - A. the title commitment.
  - B. the title opinion.
  - C. the owner's policy.
  - D. the chain of title.
8. Which of the following would be MOST concerned with and interested in recording a mortgage?
  - A. Title insurance company
  - B. Grantor
  - C. Mortgagor
  - D. Mortgagee
9. A mortgagee's title insurance policy protects
  - A. the lender.
  - B. the borrower.
  - C. the grantor.
  - D. the grantee.
10. A second mortgage can be distinguished from a first mortgage by the date the mortgages were
  - A. acknowledged.
  - B. given.
  - C. recorded.
  - D. delivered and accepted.
11. In MOST cases, for a deed to be recorded, it must be
  - A. acknowledged.
  - B. signed by the grantee only.
  - C. valid.
  - D. signed by both the grantor and grantee.

12. A deed that has NOT been recorded lacks
  - A. competent parties.
  - B. constructive notice.
  - C. actual notice.
  - D. a valid document.
13. Title insurance premiums are paid
  - A. once, at closing.
  - B. monthly, with the mortgage payment.
  - C. semiannually, with the property taxes.
  - D. annually, with the homeowners insurance premium.
14. Which of the following would give a buyer the MOST protection against losses resulting from title defects?
  - A. Mortgage default insurance
  - B. Owner's title insurance policy
  - C. Mortgagee's title insurance policy
  - D. Abstract of title
15. When a buyer records the deed from the seller, the legal consequence is to
  - A. transfer title.
  - B. give the seller assurance of holding a first lien.
  - C. serve as constructive notice of the buyer's ownership interest.
  - D. protect the seller from existing adverse claims.
16. Before closing on the purchase of a duplex, the buyer asked his attorney to render a title opinion. The attorney's title opinion will do all of the following EXCEPT
  - A. guarantee the buyer obtains marketable title.
  - B. disclose unreleased liens against the property.
  - C. disclose personal judgments against the seller.
  - D. disclose the amount and status of property taxes and special assessments.
17. Jacobson deeds property to Keene, who neither records the deed nor takes possession of the property. Jacobson later deeds the same property to Linder, who records the deed and takes possession of the property. Linder is not aware of the earlier conveyance to Keene. Who holds legal title to the property?
  - A. Jacobson, because Keene did not record her deed
  - B. Keene, because her deed is dated first
  - C. Linder, because his deed was recorded first
  - D. Keene and Linder are tenants in common, because the form of ownership was not specified in either deed
18. The BEST way for a seller to provide marketable title to real property is
  - A. to give the buyer an abstract.
  - B. to buy an owner's title policy for the buyer.
  - C. to provide a general warranty deed.
  - D. through a quiet title action.
19. The owner of a large land parcel has received a claim from a distant relative's spouse regarding ownership of the parcel, and a neighbor disputes the property line, which is shown in conflicting locations on plat documents. What may be the MOST appropriate action for the landowner?
  - A. Ask a real estate agent for advice
  - B. Consult an attorney
  - C. Sue the previous owner
  - D. File liens against the relative and the neighbor
20. Which phrase BEST describes an abstract of title?
  - A. Opinion of title
  - B. Title report
  - C. Title insurance
  - D. Historical summary
21. What does the purchase contract require the seller to deliver to the buyer at closing?
  - A. Title opinion
  - B. Title report
  - C. Marketable title
  - D. Abstract of title
22. The time period between the title insurance commitment and the recordation of the deed is known as
  - A. the gap period.
  - B. adverse possession.
  - C. the probate period.
  - D. constructive notice.
23. The best way to avoid worries about a transfer of title to real estate is to obtain which of the following?
  - A. Abstract of title
  - B. Attorney's opinion of title
  - C. Title insurance
  - D. Deed of trust

# UNIT 7 BROKER-LEVEL QUESTIONS

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1. An investor is buying a partially renovated property in “as is” condition, and plans to complete the needed work and then sell the home. The seller has agreed in the purchase contract to provide the buyer with an extended title insurance policy at closing. The title commitment shows there are two mechanics’ liens against the property and unpaid property taxes. At closing, who will be responsible for paying off these liens?
  - A. The buyer, because the buyer is purchasing it “as is”
  - B. The seller, because the liens are for work done on the property
  - C. They can be left in place for the new buyer/ investor to assume
  - D. The title company, because it found the liens after the policy was ordered
2. A chain of title is BEST described as
  - A. all the records created in the sale of a property.
  - B. the recorded documents listed in a title commitment.
  - C. a historical summary of recorded documents for a property.
  - D. the recorded documents from patent to the current title holder.
3. The main purpose of recording documents is BEST described as
  - A. a race to the courthouse to be first in time.
  - B. the best method to guarantee marketable title.
  - C. a way to create public notice and a record of legal documents.
  - D. the system to create actual notice for buyers.

# UNIT 7 QUIZ ANSWERS

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1. **D** The answer is a property history of successive conveyances and recorded interests. The chain of title links the present owner to all previous owners of the property.
2. **C** The answer is Torrens system. Only a few states verify title and then issue a Torrens certificate.
3. **B** The answer is recording real estate documents provides constructive notice of their contents to the public. Not all real estate documents have to be recorded to be valid (e.g., an unrecorded deed can transfer title to a grantee). Recording provides constructive notice of the contents of a document to the public at large.
4. **C** The answer is state law. Recording requirements are set by state statutes (laws).
5. **A** The answer is a mortgagee's title insurance policy. To protect their interests, lenders generally require a borrower to purchase a mortgagee's title insurance policy (also called a lender's policy or a loan policy).
6. **B** The answer is encroachments. Standard coverage title insurance does not protect against claims involving surveys or encroachments, or other problems that would only be discovered through an inspection of the property.
7. **D** The answer is the chain of title. The examiner is seeking an unbroken chain of title. Any gap in the ownership chain is a serious cloud on title.
8. **D** The answer is mortgagee. The mortgagee (lender) wants to make certain that the mortgage is recorded, to provide notice of the mortgagee's lien against the property.
9. **A** The answer is the lender. A lender (mortgagee) requires the borrower to purchase a mortgagee's title insurance policy to protect the lender's security interest in the property.
10. **C** The answer is recorded. Priority of rights is determined by the date of public notice. Recording a document provides constructive (public) notice.
11. **A** The answer is acknowledged. Most states require the grantor's signature on a deed to be acknowledged (notarized) to be recorded.
12. **B** The answer is constructive notice. A deed that has not been recorded lacks constructive notice, which is also known as legal notice.
13. **A** The answer is once, at closing. Title insurance policies protect against title flaws that already exist but have not yet been discovered. Therefore, the title company charges only one premium, which is typically paid at closing.
14. **B** The answer is owner's title insurance policy. The best protection for a property buyer is an owner's title insurance policy.
15. **C** The answer is serve as constructive notice of the buyer's ownership interest. Recording serves constructive notice (also called legal notice) of interests in real property.
16. **A** The answer is guarantee the buyer obtains marketable title. An attorney's title opinion does not guarantee marketable title.
17. **C** The answer is Linder, because his deed was recorded first. In a race/notice recording system, subsequent purchasers who record their deed first have good title to the property, as long as they did not have actual notice of the earlier conveyance.
18. **B** The answer is to buy an owner's title policy for the buyer. An owner's title policy is the best proof of marketable title. An abstract must have a title opinion. A general warranty deed does not prove the title is marketable, and a suit for quiet title is used to remove clouds from title.

19. **B** The answer is consult an attorney. The attorney can bring an action to quiet the title, and the court will order all parties to provide evidence of their claim and recognize valid claims.
20. **D** The answer is historical summary. An abstract of title is a chronological line-item summary of all recorded documents affecting a particular parcel.
21. **C** The answer is marketable title. The buyer's goal is to obtain marketable title, which is title free from reasonable doubt.
22. **A** The answer is the gap period. Something that affects title could happen after the title insurance company commits to the policy but before closing or deed recordation. Gap coverage is a form of title insurance that covers this gap.
23. **C** The answer is title insurance. While an abstract of title is useful, a title insurance policy will protect the buyer if a claim arises that would not have been revealed by examination of the public record.

### Broker-Level Questions

1. **B** The answer is the seller, because the liens are for work done on the property. The seller is responsible for paying off all liens incurred before closing, and mechanics' liens take priority from the day the work was done. The property taxes are already in first position, which would mean the investor could not get a loan because lenders will not allow this type of lien to have priority over a loan. The title company would be responsible if the liens were found after the policy was issued. A new buyer would not take title with these liens.
2. **D** The answer is the recorded documents from patent to the current title holder. The chain of title is created by the recording of all documents from when the government gave or sold the land to an individual, typically a patent, to the present. Both an abstract and title commitment are based on the chain of title.
3. **C** The answer is a way to create public notice and a record of legal documents. The main purpose of recording is to create a system for all legal documents, not just real estate, to be shown to the public, and to create legal or constructive notice. A race to the courthouse may or may not be a requirement for recording because each state sets its own rules.

# UNIT 8

## Real Estate Brokerage

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the fundamentals of real estate brokerage and licensing laws.
- › Describe the purpose and basic elements of antitrust laws that affect real estate practice such as price fixing, boycotts, and allocation of markets.
- › Discuss the services provided to real estate practitioners by professional organizations, including the creation and enforcement of ethical codes.
- › Explain how real estate professionals can use technology in real estate practice to comply with laws and ethical standards.

### KEY POINTS—UNIT 8

- Brokerage firms, brokers, and salespersons are referred to as real estate agents or real estate licensees.
- Consumers hire brokerage firms to help them buy, sell, or rent property.
- A brokerage firm is run by a broker, who may hire salespersons or other brokers as sales associates to carry out the duties of the brokerage firm.
- Sales associates acquire listings and buyer/tenant representation agreements on behalf of the brokerage firm. The brokerage firm owns all the representation contracts.
- The employing broker (principal broker) is responsible for training and supervising all sales associates and providing each with a written manual of the firm's policies and procedures.
- Sales associates are typically hired as independent contractors, meaning they have a contract stating that they set their own hours and are responsible for paying their own taxes.
- If a brokerage hires a sales associate as an employee, the brokerage must withhold income taxes from the sales associate's earnings.

- Licensees are expected to have a higher level of knowledge and competency than unlicensed persons.
- Licensees are not allowed to give legal advice on any aspect of a real estate transaction.
- Real estate agents should know when to recommend the use of attorneys, accountants, tax preparers, home inspectors, and other appropriate professionals to buyers and sellers.
- Commissions are determined by negotiation between the client and the brokerage. Price-fixing is the illegal practice of conspiring to charge a fixed price or commission rate. Price-fixing is a violation of the Sherman Antitrust Act, as well as state laws.

## I. BROKERAGE AND REAL ESTATE LICENSE LAWS

### A. Introduction

1. All 50 states, the District of Columbia, and all Canadian provinces license and regulate real estate professionals.
2. The terms *agent*, *real estate agent*, and *licensee* refer to all entities holding a real estate license.
  - a. Brokerage firms, brokers, and salespersons
3. Buyers, sellers, landlords, and tenants hire \_\_\_\_\_ for representation.
  - a. The brokerage firm hires sales associates, who may be licensed as salespersons or brokers, to help the firm represent its clients.
  - b. Depending on state laws, licensees hired by brokerage firms are referred to as salespersons, broker-associates, limited brokers, associate brokers, or sales associates.

### B. Real estate brokerage

1. The brokerage firm \_\_\_\_\_ and is responsible for \_\_\_\_\_.
  - a. Listings, buyer representation contracts, property management agreements, and purchase contracts
2. The employing broker (principal broker) is responsible for the following:
  - a. Training and supervising all sales associates
  - b. Creating a written office policy

### C. Relationship of broker and sales associate

1. The sales associate represents the employing broker and brokerage firm
  - a. The sales associate owes duties to the client equivalent to the duties owed by the broker



2. For tax purposes, a sales associate can be an employee or an independent contractor.
  - a. If an employee, the brokerage
    - i. \_\_\_\_\_ from the sales associate's pay; but
    - ii. does not have to guarantee vacation, a set schedule, or a specific number of hours.
  - b. An independent contractor working for the firm must
    - i. have a \_\_\_\_\_ independent contractor agreement that states they
      - may set their \_\_\_\_\_, and
      - must pay their own taxes.
  - c. The firm can require independent contractors to conform to office policies. The real estate license law will always make the broker responsible for the conduct of sales associates.

## II. ANTITRUST LAWS

### A. Price-fixing

1. Price-fixing is the conspiring between businesses to establish fixed fees or prices for services.
2. Price-fixing with other firms or associations violates the federal Sherman Antitrust Act.
3. Fees and commissions charged to the public are \_\_\_\_\_.
4. Each \_\_\_\_\_.
  - a. Brokerage firms may require all brokers and salespersons within the firm to charge a set commission.
  - b. Employing brokers establish the standard fee charged by the firm and may allow some broker-associates or salespersons to negotiate that fee with the consumer within certain parameters.
  - c. Licensees may not discuss commissions with any licensees \_\_\_\_\_ of their own firm.
5. Commissions \_\_\_\_\_ or agreement among brokerage firms, MLS systems, broker-associates, REALTOR® associations, or the state licensing authority.
  - a. The MLS does not set commissions or co-op fee amounts.
  - b. Commissions are negotiated between the listing brokerage and the seller.

**B. Additional violations**

1. Brokerage firms may not collude to boycott certain businesses.
2. Allocation of customers or \_\_\_\_\_ is prohibited.
3. Tie-in agreements are prohibited.

**C. Penalties**

1. Federal penalties for violation of the Sherman Antitrust Act can be as high as
  - a. a \_\_\_\_\_ fine and 10 years in prison for an individual;
  - b. a \_\_\_\_\_ fine for a corporation.

**III. PROFESSIONAL ORGANIZATIONS AND ETHICS**

- Ethics are moral principles, rules, and standards of conduct.

**A. Expectations of brokers and salespersons**

1. Exhibit a higher level of knowledge and competency than unlicensed persons
2. Protect the interests of clients
  - a. Treat all parties fairly and honestly
3. Complete all state-mandated disclosures in a timely fashion
4. Fully explain to the client the obligations of the client and the real estate professional
5. Disclose all material facts in a timely manner without fraud or misrepresentation

**B. Disclosure and practicing within levels of competence**

1. All real estate professionals are expected to know when they are \_\_\_\_\_ to perform a task. This includes the following:
  - a. Practicing outside their area of expertise (e.g., a residential broker selling commercial property, or an urban broker selling agricultural land)
  - b. Completing and presenting legal documents that are not fully understood by the licensee
2. Licensees become competent by completing education and working with others who are knowledgeable in the area of practice.
3. Real estate professionals are expected to fully disclose the following:
  - a. That they are a licensee and the name of their brokerage
  - b. Who they represent in the transaction

- c. The obligations of all parties, in regard to disclosure of material defects
- d. If they are a principal in the transaction
- e. If there may be any environmental, material, or other issues requiring disclosure that might impact the property

### **C. Illegal practice of law**

- 1. Real estate professionals must know when to recommend the parties they are working with seek legal advice.
- 2. Real estate professionals should recommend the use of attorneys, accountants, tax preparers, home inspectors, and other appropriate professionals to buyers and sellers.
- 3. Licensees are not allowed to give legal advice on any aspect of real estate transactions.

## **IV. TECHNOLOGY IN REAL ESTATE PRACTICE**

### **A. Communication in a digital age**

- 1. Smart phones allow conversations and text messaging, as well as \_\_\_\_\_ and \_\_\_\_\_.
- 2. Social media provide a method of communication as well as \_\_\_\_\_.

### **B. Internet advertising**

- 1. Federal and state laws must be followed. At a minimum, this includes the following:
  - a. Real estate professional's \_\_\_\_\_ must be disclosed on all website pages that include an advertisement.
  - b. Posting of a sales associate's name must include the \_\_\_\_\_.
  - c. An \_\_\_\_\_ must contain true and current information and not be \_\_\_\_\_.

### **C. Electronic contracting**

- 1. Controlled by the following two federal laws:
  - a. Uniform \_\_\_\_\_ Act (UETA)
    - i. If a state's law requires a signature on a contract, an \_\_\_\_\_ is sufficient.
    - ii. If a state's law requires a \_\_\_\_\_, an electronic record is sufficient.

- b. Electronic \_\_\_\_\_ in Global and National Commerce Act (E-Sign)
  - i. Applies in states that have not enacted the UETA
  - ii. Makes contracts (including \_\_\_\_\_) legally enforceable
- 2. All parties must be comfortable with the method of communication chosen.

**D. Prohibited communications**

- 1. The National Do Not Call Registry provides a list of phone numbers that telemarketers are not allowed to call.
  - a. Real estate professionals must check the list before cold calling potential clients.
  - b. May contact consumers up to \_\_\_\_\_ after the consumer has made an inquiry
  - c. Real estate professionals may call consumers with whom they have an established business relationship for \_\_\_\_\_ after their last transaction.
- 2. Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 (CAN-SPAM Act)
  - a. Created to reduce \_\_\_\_\_ (spam)
  - b. Email solicitations must include a means by which recipients can \_\_\_\_\_ from future messages
- 3. Children's Online Privacy Protection Act (COPPA)
  - a. Requires posting a \_\_\_\_\_ policy
  - b. Limits \_\_\_\_\_ that can be collected from children younger than 13

## UNIT 8 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

antitrust	experience and expertise	salespersons/
brokerage firm	illegal practice of law	broker-associates
collude	independent contractors	Sherman Antitrust Act
competent	negotiation	supervision
employees	office policy	withhold
ethics		

1. Commissions charged by brokerage firms for their services are set by \_\_\_\_\_.
2. \_\_\_\_\_ set their own work hours and pay their own taxes.
3. Real estate professionals must know when to recommend that the parties they are working with seek legal advice so as to avoid the \_\_\_\_\_.
4. The employing broker (principal broker) is responsible for creating a written \_\_\_\_\_.
5. Brokerage firms may not \_\_\_\_\_ to boycott certain businesses, establish rates paid to salespersons or broker-associates, or assign specific territories or price ranges.
6. \_\_\_\_\_ refers to a system of moral principles, rules, and standards of conduct.
7. Buyers, sellers, landlords, and tenants hire the \_\_\_\_\_ for representation.
8. All listing, buyer, tenant, and landlord representation contracts belong to the \_\_\_\_\_.
9. Brokerage firms must create a written \_\_\_\_\_ and provide training and \_\_\_\_\_ for all licensees and employees associated with the firm.
10. Clients are represented by a brokerage firm that hires \_\_\_\_\_ to represent the brokerage firm in assisting its clients.
11. A brokerage firm hiring licensees as \_\_\_\_\_ must withhold taxes from the employee's pay.
12. Real estate professionals are expected to know when they are not \_\_\_\_\_ to perform certain tasks, such as taking a listing that is outside of their area of \_\_\_\_\_.
13. If brokerage firms \_\_\_\_\_ to boycott a certain business, establish a fixed commission rate, or assign territories in a given market area, they have violated the \_\_\_\_\_.

## UNIT 8 GLOSSARY REVIEW ANSWERS

1. negotiation
2. Independent contractors
3. illegal practice of law
4. office policy
5. collude
6. Ethics
7. brokerage firm
8. brokerage firm
9. office policy, supervision
10. salespersons/broker-associates
11. employees
12. competent, experience and expertise
13. collude, Sherman Antitrust Act

# UNIT 8 QUIZ

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1. A consumer on the National Do Not Call Registry may be contacted by a real estate professional if the consumer made an inquiry within the last
  - A. 3 months.
  - B. 6 months.
  - C. 12 months.
  - D. 18 months.
2. The amount of commission paid to a brokerage is established by
  - A. state law.
  - B. negotiation between the brokerage and its clients.
  - C. local custom.
  - D. real estate boards.
3. A brokerage firm that hires salespersons as independent contractors should supply them with
  - A. set work schedules.
  - B. paid vacations.
  - C. notice of the brokerage firm's withholding for taxes.
  - D. a contract that states salespersons pay their own taxes and set their own hours.
4. All of the following are true EXCEPT
  - A. a group of brokerage firms cannot make agreements to avoid using a certain title company.
  - B. commissions may be set by the brokerage firm and then negotiated by a company broker or salesperson with a buyer or seller.
  - C. commissions are typically set by the MLS and boards of REALTORS® and then finalized by the brokerage firm.
  - D. a group of brokerage firms may not make agreements to list properties only in certain territories.
5. Real estate agents need to know who is required to sign each document, the importance of marketable title, how ownership issues may impact title transfer, and the essential elements of deeds and contracts because agents must
  - A. give legal advice to their clients throughout the transaction.
  - B. know what makes documents valid to avoid unnecessary delays.
  - C. provide title opinions and title reports.
  - D. advise all parties on legal issues.
6. Which statement is TRUE about the National Do Not Call Registry law?
  - A. It has little, if any, impact on the real estate business.
  - B. It requires an option to opt out and a 30-day notice to the consumer.
  - C. It should be followed by all real estate professionals.
  - D. It requires registration to avoid fines.
7. Conspiring between businesses to establish fixed fees or prices for services is illegal and is known as
  - A. a group boycott.
  - B. negotiating commissions.
  - C. dividing territory.
  - D. price-fixing.
8. Which statement is TRUE?
  - A. Each brokerage firm establishes its own commission rates.
  - B. The MLS determines the commission that member brokerages may charge.
  - C. Brokerage firms may discuss commissions with other firms at REALTOR® Association events.
  - D. Salespersons determine commission rates.
9. Which of the following is NOT an appropriate listing for most first-year agents?
  - A. Single-family home
  - B. Residential lot
  - C. Multi-tenant retail property
  - D. Vacation home

10. Ethical and fiduciary expectations require real estate licensees to practice all of the following EXCEPT
  - A. exhibit a higher level of knowledge and competency than unlicensed persons.
  - B. disclose confidential material facts to clients only.
  - C. protect the interests of clients.
  - D. treat all parties fairly and honestly.
11. Real estate professionals are expected to know when they are NOT competent to perform a task, such as
  - A. practicing outside their area of expertise.
  - B. completing and presenting legal documents not fully understood by the licensee.
  - C. disclosing construction defects to buyers against the client's will.
  - D. both practicing outside their area of expertise and completing and presenting legal documents not fully understood by the licensee.
12. A real estate agent is expected to
  - A. disclose that they are a licensee, the name of their brokerage, and who they represent.
  - B. discuss commission rates of other brokerages.
  - C. disclose the client's confidential information.
  - D. avoid showing properties listed by discount brokerages.



# UNIT 8 BROKER-LEVEL QUESTIONS

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1. Which of these actions is permissible under the Sherman Antitrust Act?
  - A. Two principal brokers agree to pay all licensees under them only at 55:45 splits.
  - B. The board of REALTORS® agrees to not allow “fee only” firms to advertise in the MLS.
  - C. The MLS system offers the buyer’s brokerage firms a co-op fee that is paid by the listing brokerage to the buyer’s brokerage.
  - D. A group of local brokers agrees to have each firm exclusively market in separate areas of the city.

# UNIT 8 QUIZ ANSWERS

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1. **A** The answer is three months. National Do Not Call Registry rules state that real estate professionals may contact consumers for three months after the consumer has made an inquiry.
2. **B** The answer is negotiation between the brokerage and its clients. Each brokerage establishes its own commission rate, but brokerages cannot collude to establish a fixed rate.
3. **D** The answer is a contract that states salespersons pay their own taxes and set their own hours. The IRS requires real estate agents hired as independent contractors to have a contract stating that they set their own hours and pay their own taxes.
4. **C** The answer is commissions are typically set by the MLS and boards of REALTORS® and then finalized by the brokerage firm. Commissions may not be set by law, the MLS, or anyone outside the brokerage firm. Doing so is a violation of the Sherman Antitrust Act. The brokerage firm may set commissions and policies that allow company brokers or salespersons to then negotiate commissions with buyers and sellers.
5. **B** The answer is know what makes documents valid to avoid unnecessary delays. Real estate agents can avoid aggravating delays by assuring contract documents are properly prepared and signed and identifying potential transaction problems early on.
6. **C** The answer is it should be followed by all real estate professionals. The National Do Not Call Registry law applies to the solicitation of consumers and should be followed by all real estate professionals.
7. **D** The answer is price-fixing. Price-fixing is prohibited by the Sherman Antitrust Act.
8. **A** The answer is each brokerage firm establishes its own commission rates. Conspiring between businesses to establish fixed fees or prices for services is price-fixing and is illegal, so brokerages must set their own commissions.
9. **C** The answer is multi-tenant retail property. Most first-year agents lack the competency required to adequately represent sellers of income-producing commercial properties.
10. **B** The answer is disclose confidential material facts to clients only. Licensees are required to disclose material facts to all parties to a transaction.
11. **D** The answer is both practicing outside their area of expertise and completing and presenting legal documents not fully understood by the licensee. Construction defects are material facts that must be disclosed regardless of the client's will, so competence in that matter is not in question. Practicing within an area of expertise and fully understanding legal documents in the real estate transaction are critical aspects of competence.
12. **A** The answer is disclose that they are a licensee, the name of their brokerage, and who they represent. How and when these and other disclosures are to be made is determined by state laws.

## Broker-Level Questions

1. **C** The answer is the MLS system offers the buyer's brokerage firms a co-op fee that is paid by the listing brokerage to the buyer's brokerage. Co-op fees are paid by the listing firm as agreed to by the seller and the listing broker. Principals may not set fees with other brokers for commissions or splits paid to associates or salespeople. The MLS must allow all brokerage firms who are members access to the MLS and cannot deny membership based on how the firm is paid. Brokerage firms may not agree to split up where they work in the city to avoid competition.

# UNIT 9

## Real Estate Agency

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain agency concepts and terminology.
- › Explain express and implied agency and an agent's fiduciary duties.
- › Define the types of agency and identify which, if any, are involved in real estate practice.
- › Describe an agent's duties to third-party customers, especially regarding misstatements, misrepresentation, and potential fraud.

### KEY POINTS—UNIT 9

- This unit covers the common law of brokerage representation. Each state further refines the laws and rules of conduct required of agents.
- An agent is a person who is employed to represent or act for someone else (the *principal*) in dealings with third parties.
- The common law of agency creates a fiduciary relationship. The agent's fiduciary duties to the principal include the duties of care, obedience, loyalty, disclosure, accounting, and confidentiality (COLD-AC).
- Depending on the degree of authority conferred by the principal, an agent may be a special agent, general agent, or universal agent. In most cases, the real estate brokerage firm is a client's special agent, while a sales associate is an employing broker's general agent.
- A dual agent represents both the buyer and the seller at the same time. If state law permits it, dual agency is only allowed if both parties consent to the arrangement in writing.
- Every licensee is required to disclose existing brokerage relationships to third parties or their agents. State laws often require that this disclosure be in writing before the real estate professional receives any confidential information from a member of the public.

- State law determines the types of representation the brokerage firms in that state will be able to offer buyers and sellers. These types of representation include single agency, dual agency, and a variety of nonagency relationships.
- An agency relationship may be terminated by accomplishment of purpose, expiration of the term of relationship, agreement, breach by one of the parties, or operation of law.
- Trust funds (money held for someone else) include earnest money, rents, and security deposits and must be kept separate from brokerage funds.
- An agent's primary responsibility is to the principal, but the agent also owes duties to third parties.
- Most states require the seller of residential property to complete a seller's property condition disclosure statement.
- Megan's Law requires the states to have a system for the registration of sex offenders.

## I. HISTORY OF AGENCY

### A. Three sources of agency law

1. Common law consists of the rules established by tradition and \_\_\_\_\_.
2. Statutory law includes the laws established by the \_\_\_\_\_.
3. Administrative law includes the rules and regulations created by \_\_\_\_\_ as authorized by the legislature.

### B. Parties to an agency relationship

1. Principal: one who employs another to act on their behalf
  - a. May or may not be the person who pays the agent
2. An agent is the individual who is authorized and consents to \_\_\_\_\_ of another person in dealings with a third person.
3. Agency is the \_\_\_\_\_ between principal and agent.
4. The agent is held in a position of special trust and confidence by the principal because the agent is a \_\_\_\_\_.
5. The client is the \_\_\_\_\_ in a real estate transaction for whom a real estate broker acts as agent.
6. A third party or nonrepresented consumer is not a principal but a person for whom some level of service may be provided and who is entitled to \_\_\_\_\_. The third party may be represented by a separate agent.
7. A nonagent may also be referred to as a facilitator, intermediary, transactional broker, transaction coordinator, or contact broker. This person works with a buyer and seller (or landlord and tenant), assisting with the transaction \_\_\_\_\_ representing either party's interests.

## II. CREATION OF AGENCY

### A. Key points

1. Agency is determined by who \_\_\_\_\_ the agent.
2. An express agency is created by an \_\_\_\_\_.
  - a. A listing agreement is a \_\_\_\_\_.
  - b. An express agency relationship between a buyer and a broker is created by a \_\_\_\_\_.
  - c. Only written agency agreements are enforceable.
  - d. An \_\_\_\_\_ agency is created through an agent's actions, such as by providing advice to a third party.
3. The source of \_\_\_\_\_ does not determine agency.

### B. Fiduciary responsibilities

1. The agent owes the principal the duties of care, obedience, loyalty, disclosure, accounting, and \_\_\_\_\_ (COLD-AC).
2. An agent must obey the \_\_\_\_\_ directions of the principal.
3. \_\_\_\_\_ means an agent must place the interest of the principal above all others.
4. The duty of disclosure includes all facts or information that might \_\_\_\_\_.
5. The duty of accounting means that \_\_\_\_\_ client monies with the agent's personal or business funds is always illegal.
6. The agent's duty of confidentiality lasts as long as dictated by \_\_\_\_\_ or, as required by the National Association of REALTORS®, \_\_\_\_\_.

## III. TYPES OF AGENCY RELATIONSHIPS

### A. Classified by extent of agent's authority

1. A \_\_\_\_\_ agent is empowered to do anything the principal could do personally.
2. A \_\_\_\_\_ agent may represent the principal in a broad range of matters related to a particular business or activity.
3. A \_\_\_\_\_ agent, also called a \_\_\_\_\_ agent, represents the principal in one specific act or business transaction only.
4. A real estate broker usually acts as a \_\_\_\_\_ for a client.

**B. Disclosure of agency**

1. Mandatory agency disclosure laws exist in \_\_\_\_\_.
2. There may be a specific disclosure form that the real estate agent is required to use.

**C. Single agency**

1. A single agent represents only one party to a transaction. The \_\_\_\_\_ is the party not represented by the agent.
2. Dual agency occurs when a brokerage firm represents more than one party to a transaction.
  - a. Limits the level of representation licensees can provide
  - b. Prohibits acting exclusively for either party
  - c. Requires \_\_\_\_\_ of both parties
3. Some states allow two sales associates of the same brokerage to represent clients with opposing interests in the same transaction as \_\_\_\_\_ without creating a dual agency conflict.
4. Some states allow a real estate licensee to take part in a transaction as a \_\_\_\_\_ of either party.
  - a. The agent assists the parties with paperwork and the formalities of the transaction in what are termed \_\_\_\_\_.
  - b. The \_\_\_\_\_ may be called a transaction broker, facilitator, transaction coordinator, or contract broker.
5. An agency may be terminated by
  - a. Completion, performance, or fulfillment of the agency's purpose
  - b. Death or \_\_\_\_\_ of either party
  - c. Destruction or condemnation of \_\_\_\_\_
  - d. Expiration of the terms of the agency
  - e. Mutual agreement by \_\_\_\_\_ to cancel the contract
  - f. \_\_\_\_\_ by one of the parties
  - g. Operation of \_\_\_\_\_, as in a bankruptcy of the principal

## IV. CUSTOMER-LEVEL SERVICES

### A. Key points

1. When dealing with a customer—the third party to the agency—the real estate professional's responsibilities include the following:
  - a. Reasonable \_\_\_\_\_ in performance of the agent's duties
  - b. Honest and fair dealing
  - c. Disclosure of \_\_\_\_\_ the real estate professional knows or should reasonably be expected to know that materially affect the \_\_\_\_\_ of the property
2. Care must be taken to avoid making a representation about a property that could be deceptive. Even if not deliberate, the agent must not make a \_\_\_\_\_.

### B. Disclosures

1. Most states require the seller of residential property to complete a \_\_\_\_\_ statement.
  - a. The disclosure may be a statutory form or a written list.
  - b. The disclosure typically covers the following:
    - i. Land/soil and environmental conditions
    - ii. Structural issues and condition of fixtures, appliances, and equipment
    - iii. Lot size, encroachments, easements, and so on
    - iv. All material defects
  - c. \_\_\_\_\_ (never agents) complete the seller's disclosure to the best of their \_\_\_\_\_.
  - d. Sellers and licensees must disclose visible and known latent material defects to all buyers.
    - i. A material fact or defect is one that, if known, \_\_\_\_\_.
    - ii. A latent defect is a \_\_\_\_\_ that is not easily discovered by an inspection.
  - e. State laws determine when the buyer should receive the disclosure.
  - f. Buyers may be able to rescind the contract if they can prove misrepresentation.

2. Most states require brokers to visually inspect the property. Listing agents must do the following:
  - a. Disclose all known material defects, regardless of the seller's awareness of the defect or instructions to not disclose
  - b. Request the seller disclose any known latent (hidden) defects
  - c. Upon discovery of a material defect,
    - i. immediately disclose to the client, then
    - ii. disclose to all parties to the transaction
  - d. Recommend that buyers have the property inspected
3. Agent responsibility for seller misrepresentation
  - a. If a seller misrepresents a latent defect in the seller's property disclosure and
    - i. the broker performed a visual inspection not finding any obvious defects, then
    - ii. the seller (not the agent) could be held responsible for misrepresentation.

### **C. Stigmatized properties**

1. The value of some properties is affected by something that happened on the property or its proximity to a nuisance.
2. State law on the issue should be learned and followed.

### **D. Megan's Law**

1. Megan's Law is a federal law that requires the registration of sex offenders.
2. Real estate professionals should inform buyers concerned about the possible presence in the area of any registered sex offender to contact local law enforcement offices.
3. The obligation to disclose and inform buyers varies by state.



## UNIT 9 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

agent	facilitator	Megan's Law
brokerage firm	fiduciary	principal
buyer	general	seller
commingling	immediately	third party
contact local	listing contract	transaction broker
conversion	local	trust account
dual	loyalty	written agreement
errors and omissions	material facts	

1. One who employs an agent to act on their behalf is a(n) \_\_\_\_\_.
2. The person or company employed to act on behalf of the principal is a(n) \_\_\_\_\_.
3. The relationship between the brokerage and principal is a(n) \_\_\_\_\_ relationship.
4. When a brokerage serves as the agent for the \_\_\_\_\_ and the seller in the same transaction, a(n) \_\_\_\_\_ agency exists.
5. Depositing a client's money in the same account with the broker's money (which is illegal) is \_\_\_\_\_.
6. Agency is established through an express \_\_\_\_\_.
7. Real estate commissions charged by a firm are determined by the \_\_\_\_\_.
8. A licensee providing services without agency representation is a(n) \_\_\_\_\_ / \_\_\_\_\_.
9. A(n) \_\_\_\_\_ is an agency employment agreement in which the \_\_\_\_\_ hires a \_\_\_\_\_ to help sell a property.
10. The fiduciary duty of \_\_\_\_\_ means that an agent must place the principal's best interest above all others, including the agent's.
11. An agent's duty to a \_\_\_\_\_ includes disclosure, accounting, honesty, and fair dealing.
12. Real estate agents and residential sellers must disclose all \_\_\_\_\_ and latent defects to all buyers.
13. To comply with \_\_\_\_\_, states must establish a registry of sex offenders.
14. Real estate professionals should inform buyers concerned about a registered sex offender to \_\_\_\_\_ law enforcement offices.

## **UNIT 9 GLOSSARY REVIEW ANSWERS**

1. principal
2. agent
3. fiduciary
4. buyer, dual
5. commingling
6. written agreement
7. brokerage firm
8. facilitator, transaction broker
9. listing contract, seller, brokerage firm
10. loyalty
11. third party
12. material facts
13. Megan's Law
14. contact local

# UNIT 9 QUIZ

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1. When acting in an agency capacity, a listing brokerage is
  - A. the seller's agent.
  - B. the buyer's principal.
  - C. the buyer's agent.
  - D. the third party.
2. The document used to form the relationship between the agent and the principal is
  - A. an open listing.
  - B. a fiduciary agreement.
  - C. a facilitations contract.
  - D. a lease.
3. A brokerage deposits trust funds into the firm's operations account. This is an example of
  - A. conversion.
  - B. commingling.
  - C. proper accounting.
  - D. fraud.
4. If a broker and a seller have a fiduciary relationship, the broker could
  - A. inform a buyer that the seller will accept substantially less than the listed price.
  - B. fail to tell the buyer about hidden structural problems to protect the seller.
  - C. disclose the buyer's financial qualifications.
  - D. honor the seller's request to refuse to show the property to minorities.
5. A seller informs a salesperson that a house is for sale "as is." The salesperson should
  - A. inform all potential buyers that there is nothing wrong with the property even though the salesperson has not inspected it.
  - B. visually inspect the property, and if the salesperson sees a water leak in the ceiling, the salesperson should disclose that information to potential buyers.
  - C. allow the seller to handle all conversations with potential buyers about the condition of the property.
  - D. advise potential buyers that an "as is" property requires no property disclosures.
6. When a property manager signs a property management contract with an owner, the property manager is
  - A. a general agent of the property owner.
  - B. a third party to the contract.
  - C. a universal agent of the broker.
  - D. a principal of the property owner.
7. While showing an income-producing property, the broker advised the consumer that the property is likely to be very profitable in the future because of its location. The broker's actions might result in the creation of
  - A. universal agency.
  - B. general agency.
  - C. ostensible agency.
  - D. implied agency.
8. A real estate professional acting solely as a seller's agent is MOST likely to be held liable for claims of misrepresentation by a buyer if the agent committed which of these acts in the course of the transaction?
  - A. Failed to provide previous purchase prices for the property
  - B. Obeyed the seller's instructions to leave all discussions of property condition to the seller
  - C. Continued to accept and present offers on the property after the seller accepted the buyer's offer
  - D. Deposited the earnest money check in a personal account to clear before transferring it to the trust account
9. A real estate agent's fiduciary obligation does NOT include
  - A. acting as an advocate.
  - B. obedience and loyalty.
  - C. disclosure of confidential information about the principal.
  - D. disclosure of all risks and benefits of the transaction.

10. What duties does a listing agent owe to a third-party buyer?
  - A. Fairness and disclosure of benefits and risks
  - B. Honesty, accounting, and disclosure of material facts
  - C. Honesty, confidentiality, and fairness
  - D. Disclosure of material facts, honesty, and loyalty
11. Megan's Law requires
  - A. adherence to fiduciary duties.
  - B. agents to disclose the location of registered sex offenders.
  - C. registration of sex offenders.
  - D. neighborhood associations to identify sex offenders.
12. The buyer has received the seller's material fact disclosure and signed a purchase agreement. When does the agent's duty to disclose material facts terminate?
  - A. When the buyer received the seller's disclosure
  - B. Upon delivery and acceptance of the signed purchase agreement
  - C. When the buyer received a written report from a qualified home inspector
  - D. At closing
13. The buyer's agent notices ceiling damage and water stains in an upper-level bedroom—items that did not appear on the seller's disclosure statement. What should the agent do with this information?
  - A. Disclose immediately to the buyer and notify the listing agent
  - B. Nothing because the seller's disclosure is the only disclosure required
  - C. Do not disclose because of the agent's fiduciary duty to the seller
  - D. Disclose the information at closing
14. A fact, situation, or property defect that, if known, might change a party's decision to go forward with a transaction is
  - A. an irrelevant fact.
  - B. a material fact.
  - C. an alternative fact.
  - D. a proven fact.
15. A type of agency in which the agent is authorized to help a buyer buy or help a seller sell, but the agent cannot sign a purchase contract on behalf of the client, is
  - A. a special agency.
  - B. a general agency.
  - C. a universal agency.
  - D. an implied agency.
16. The agency relationship between a brokerage and the agents associated with the brokerage is BEST described as
  - A. a special agency.
  - B. a universal agency.
  - C. an implied agency.
  - D. a general agency.
17. Which type of agency relationship exists when an agent is authorized to perform in place of the principal with the unlimited ability to contractually bind the principal?
  - A. Special agency
  - B. General agency
  - C. Universal agency
  - D. Implied agency
18. Which type of agency could be unwittingly created by a licensee's actions, such as giving advice to a customer?
  - A. Universal agency
  - B. Implied agency
  - C. Special agency
  - D. General agency
19. Which BEST describes a universal agency?
  - A. A principal grants power of attorney to an attorney-in-fact.
  - B. An agent has limited authority to contractually bind the principal.
  - C. Authorized representation without the ability to bind contractually
  - D. All of these
20. All of the following must be deposited into the broker's trust account EXCEPT
  - A. rents.
  - B. security deposits.
  - C. commissions and fees.
  - D. earnest money.

# UNIT 9 BROKER-LEVEL QUESTIONS

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1. A listing broker brings the seller an offer from one of the broker's clients. The listing broker is acting as
  - A. a transaction broker or facilitator.
  - B. a seller's agent.
  - C. a buyer's agent.
  - D. a dual agent.
2. A neighbor visits a house during the listing broker's open house and expresses some interest in buying the home or something similar in the neighborhood. What does the listing broker owe to the neighbor?
  - A. Honest and fair answers to questions
  - B. Maintaining the neighbor's confidential information from the seller
  - C. Disclosing the benefits and risks in any transaction
  - D. The same fiduciary obligations the listing broker owes the seller

# UNIT 9 QUIZ ANSWERS

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1. **A** The answer is the seller's agent. The seller hires the listing broker to help the seller sell a property.
2. **B** The answer is a fiduciary agreement. Fiduciary agreements create the representation obligations of agents to principals.
3. **B** The answer is commingling. Trust funds must be placed in a trust account, not the broker's business/operations account.
4. **C** The answer is disclose the buyer's financial qualifications. As a fiduciary of the seller, the broker has the duties of care, obedience, loyalty, disclosure, accounting, and confidentiality (COLD-AC). However, these fiduciary duties do not require or permit the broker to commit fraud or violate antidiscrimination laws.
5. **B** The answer is visually inspect the property, and if the salesperson sees a water leak in the ceiling, the salesperson should disclose that information to potential buyers. Licensees must reveal all material facts they know or reasonably should know.
6. **A** The answer is a general agent of the property owner. Property management is an ongoing business relationship. The property manager is the general agent (fiduciary) of the property owner.
7. **D** The answer is implied agency. Acting as if you are someone's agent, such as giving advice or sharing opinions, can create an implied agency.
8. **B** The answer is obeyed the seller's instructions to leave all discussions of property condition to the seller. Regardless of the seller's instructions, agents may be charged with misrepresentation if they fail to disclose a material fact about property condition.
9. **C** The answer is disclosure of confidential information about the principal. The law of agency specifies fiduciary obligations to the principal, including loyalty, confidentiality, disclosure, obedience, reasonable care and skill (diligence), and accounting. This makes the agent an advocate for the principal.
10. **B** The answer is honesty, accounting, and disclosure of material facts. A listing agent owes a third party honesty, fairness, accounting, and disclosure of all material facts.
11. **C** The answer is registration of sex offenders. Megan's Law is a federal law that requires registration and public notification that a sex offender is living in a community.
12. **D** The answer is at closing. If the agent is aware of a material fact that was not previously disclosed to the buyer, the agent has a duty to disclose that fact up to and through the closing.
13. **A** The answer is disclose immediately to the buyer and notify the listing agent. Agents are required to disclose any errors in the seller's disclosure to their clients immediately.
14. **B** The answer is a material fact. While state laws ultimately define material facts, a fact is considered material to a transaction if knowledge of the fact would alter a party's decision regarding the transaction.
15. **A** The answer is a special agency. In a special agency, the agent is authorized to perform a particular act without the ability to bind the principal contractually.
16. **D** The answer is a general agency. In a general agency, the agent is authorized to perform a series of acts associated with the continued operation of a particular business, with a limited ability to bind the principal contractually.

17. **C** The answer is universal agency. The principal gives the agent control over all of the principal's affairs in a universal agency. Appointment of a universal agent is often part of an end-of-life plan.
18. **B** The answer is implied agency. An implied agency may be created by an agent's actions, such as giving advice to a third party.
19. **A** The answer is a principal grants power of attorney to an attorney-in-fact. An attorney-in-fact is often hired to act on behalf of the principal, should the principal become incapacitated or otherwise not be able to act on his own behalf.
20. **C** The answer is commissions and fees. Depositing sales commissions, property management fees, and funds belonging to the broker into a trust account is commingling—illegally mixing client funds and brokerage funds.

### Broker-Level Questions

1. **D** The answer is a dual agent. A listing broker who brings an offer from a client that the listing broker represents is acting as a dual agent.
2. **A** The answer is honest and fair answers to questions. The neighbor is a consumer who is owed honest and fair answers, accounting of all funds, and disclosure of the broker agency relationship and any material facts. The broker has no agency obligations to the neighbor.





# UNIT 10

## Client Representation Agreements

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the different types of listing agreements and how they may be terminated.
- › Describe the listing presentation and the information needed for a listing agreement.
- › Identify the listing agreement terms and the responsibilities of both parties.
- › Describe the types of buyer representation agreements and how they may be terminated.

### KEY POINTS—UNIT 10

- A listing (seller representation) contract is a fiduciary contract in which the owner/seller hires a brokerage firm to act as a special agent to find a buyer who is ready, willing, and able to buy according to the terms of the listing contract.
- While all listing agreements share some commonalities, state laws determine specific required content.
- In an exclusive listing, the seller hires a single brokerage to market and sell the property. An exclusive listing is a bilateral contract. There are two types of exclusive listings: exclusive right to sell and exclusive agency.
- In an exclusive right-to-sell listing, the listing brokerage is paid a commission if the property sells, regardless of who found the buyer.
- In an exclusive agency listing, the listing brokerage is NOT paid a commission if the seller finds a buyer through the seller's own efforts. The listing brokerage is paid a commission if the property sells under any other circumstances.

- In an open/nonexclusive listing, the seller can sign open contracts with more than one brokerage firm (nonexclusive). Only the brokerage that procures (finds) the buyer is paid. If the property sells, all other open listings are automatically terminated with or without notice. An open listing is a unilateral contract.
- Listing brokerages are obligated to promptly present all written offers to the seller, write an offer if so requested by an unrepresented buyer, pay fees only to their own salespersons or other licensed brokerages, market and sell the property per the terms of the listing contract, disclose material facts, and verify the buyer has received the seller's property disclosure per state laws.
- Buyer representation contracts are similar to and contain many of the same elements as a listing (seller representation) contract. Buyer representation agreements can be an exclusive right to buy or an exclusive agency contract.
- Home warranties may be offered by sellers or negotiated in an offer, and may be paid for by either party. Home warranties may cover most of a home, including all major systems and appliances, or simply cover one or more specific items (e.g., furnace, water heater, appliances).

## I. REPRESENTING THE SELLER

### A. Listing agreement (specific content determined by state law)

1. A fiduciary employment contract
  - a. The owner/seller hires a brokerage firm to act as a special agent.
  - b. The specific purpose is to find a buyer who is ready, willing, and able to buy according to the terms of the listing contract.
2. Types of listings
  - a. Exclusive right to sell
    - i. The brokerage gets paid if the property sells, regardless of who finds the buyer.
      - Even if the \_\_\_\_\_ finds a buyer for the property
    - ii. Maximum protection to brokerage; broker will give maximum effort
    - iii. Bilateral contract
  - b. Exclusive agency
    - i. The seller has no liability to pay the brokerage \_\_\_\_\_ .
    - ii. Bilateral contract
    - iii. The co-op firm will be paid if it procures the buyer.

- c. Open/nonexclusive
  - i. Only the brokerage that \_\_\_\_\_ (finds) the buyer gets paid.
  - ii. The seller can sign open contracts with more than one brokerage firm.
  - iii. Unilateral contract
  - iv. Sale to a buyer automatically terminates all other open listings with or without notice.
- d. Net listing
  - i. Specifies the net amount of money the \_\_\_\_\_ will receive from a sale
  - ii. Any amount over the specified net is paid to the broker as \_\_\_\_\_.
  - iii. Because of the inherent conflict of interest for the broker, this type of listing is \_\_\_\_\_ in many states and discouraged in others.

## **B. Listings involving cooperating brokers**

- 1. Multiple-listing clause
  - a. Authorizes brokerage to list property in the multiple listing service (MLS)
  - b. A participating broker makes a \_\_\_\_\_ offer of cooperation and compensation to other member brokers.
  - c. The offer is accepted when a \_\_\_\_\_ brings a buyer to the seller and a sale takes place.
- 2. A cooperating broker may
  - a. be a \_\_\_\_\_ of the seller,
  - b. be a \_\_\_\_\_ representative, or
  - c. act in some other capacity permitted by \_\_\_\_\_.

## **II. THE LISTING PRESENTATION**

### **A. Marketing efforts of the firm**

- 1. Marketing materials
  - a. Signage, if permitted
  - b. Flyers, mailers, other \_\_\_\_\_ pieces
  - c. Preparation of photos and videos of property
  - d. Use of MLS, if permitted
  - e. Posting on brokerage website and other \_\_\_\_\_ resources

2. Assistance with determination of listing price

- a. Broker or sales associate prepares a \_\_\_\_\_.
- b. Recently sold homes and homes currently listed for sale are \_\_\_\_\_ to the seller's property.

**B. Information needed for a listing agreement**

1. Facts about the property owner(s)

- a. \_\_\_\_\_ of owners
- b. Relationship, if any, of \_\_\_\_\_
- c. Possibility of seller financing or agreement to a \_\_\_\_\_ of the property

2. Property details

- a. Street address and \_\_\_\_\_ of the property
- b. Size, type, age, and construction of property \_\_\_\_\_
- c. \_\_\_\_\_ classification of the property
- d. Most recent \_\_\_\_\_
- e. Neighborhood \_\_\_\_\_
- f. Required \_\_\_\_\_ about property condition

**C. Disclosures**

1. Role of \_\_\_\_\_ in the transaction, in writing as required by state law
2. Property condition, as known by \_\_\_\_\_

**III. THE LISTING CONTRACT**

**A. Listing agreement provisions**

1. Names of all \_\_\_\_\_
2. Name of \_\_\_\_\_
3. Description of the \_\_\_\_\_
4. Listing \_\_\_\_\_
5. Broker's authority and \_\_\_\_\_
6. \_\_\_\_\_ compensation

7. Real property and \_\_\_\_\_
8. Leased \_\_\_\_\_
9. Proposed dates for \_\_\_\_\_
10. Information on \_\_\_\_\_
11. Evidence of \_\_\_\_\_
12. And \_\_\_\_\_ on the property
13. Whether seller or listing broker will provide a \_\_\_\_\_
14. Term of the contract and how an earlier \_\_\_\_\_ of the contract can be accomplished
15. A broker \_\_\_\_\_ clause in the event a sale is made within a stated period of time to someone introduced to the seller by the broker
16. Warranties to be made by the \_\_\_\_\_
17. Indemnification or \_\_\_\_\_ provision
18. Nondiscrimination wording in compliance with \_\_\_\_\_ laws
19. \_\_\_\_\_ provision regarding negotiability of fees
20. \_\_\_\_\_ of the parties
21. \_\_\_\_\_ the contract is signed

#### **IV. REPRESENTING THE BUYER**

##### **A. Parties to the agreement**

1. The buyer is the \_\_\_\_\_ .
2. The \_\_\_\_\_ is the agent/fiduciary.

##### **B. Same elements as listing contract**

##### **C. Can be exclusive right to buy or exclusive agency contract**

**D. Termination of agency agreements**

1. Full performance, closing, or expiration of the contract
2. Death or bankruptcy of principal or brokerage firm (not sales associate)
3. \_\_\_\_\_ of improvements (e.g., the house burns down)
4. Mutual rescission (NOT unilateral)
5. Breach by either party
  - a. Can terminate the contract (voidable); there may be liability issues

## UNIT 10 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

all owners	exclusive right-to-sell	ready, willing, and able
automatic	existing	sales associates
brokerages	expiration	special
employment	home warranties	statutory
exclusive agency	open	terminate

1. A listing contract in which the owner agrees to pay the agent a commission regardless of who sells the property during the listing period is a(n) \_\_\_\_\_ listing.
2. A buyer representation contract that appoints a brokerage as the sole agent to find a property for a buyer, but allows the buyer to find her own property without paying a commission, is a(n) \_\_\_\_\_.
3. A listing that allows an owner to list concurrently with more than one brokerage is a(n) \_\_\_\_\_ listing.
4. When working a listing with more than one owner, it is imperative that \_\_\_\_\_ sign the listing agreement.
5. By law, listings and buyer representation agreements must have a(n) \_\_\_\_\_ date and cannot contain a(n) \_\_\_\_\_ renewal clause.
6. An owner hires a real estate brokerage as a(n) \_\_\_\_\_ agent to find a buyer who is \_\_\_\_\_ to purchase the property according to the terms of the listing contract.
7. Full performance, closing, or expiration will \_\_\_\_\_ an agency agreement.
8. Buyers and sellers of existing homes can negotiate the purchase of \_\_\_\_\_ to cover the home or specific components of the home.
9. Representation agreements are fiduciary \_\_\_\_\_ agreements.
10. Sellers only pay commissions to licensed real estate \_\_\_\_\_ ; brokerages may pay only their own \_\_\_\_\_ and other brokerages.

## UNIT 10 GLOSSARY REVIEW ANSWERS

1. exclusive right-to-sell
2. exclusive agency
3. open
4. all owners
5. expiration, automatic
6. special; ready, willing, and able
7. terminate
8. home warranties
9. employment
10. brokerages, sales associates



# UNIT 10 QUIZ

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1. In an exclusive right-to-sell listing, the principal contracts
  - A. with several brokers, each of whom deals with only one third party.
  - B. to pay the broker a commission regardless of who procures the buyer.
  - C. with only one broker, but reserves the right to sell the property herself without paying a commission.
  - D. with several brokers.
2. All of the following will terminate a brokerage representation agreement without liability EXCEPT
  - A. destruction of the property.
  - B. mutual agreement.
  - C. expiration.
  - D. death of the sales associate.
3. A listing in which the principals agree to contract with only one broker but reserve the right to sell the property themselves without any liability to the brokerage for paying a commission is
  - A. an exclusive agency listing.
  - B. an open listing.
  - C. an exclusive right-to-sell listing.
  - D. a net listing.
4. The owner of a property has signed an exclusive right-to-sell listing contract. In this case, the owner
  - A. has promised to accept a reasonable offer.
  - B. has promised to accept any offer identical to the listed price and terms.
  - C. has promised to pay a commission if the property is sold during the listing period.
  - D. will pay only the brokerage who finds a buyer.
5. The clause in a listing contract that protects the broker's commission if someone with whom the broker negotiated purchases the property after the expiration of the listing is known as
  - A. a nondiscrimination clause.
  - B. a protection or safety clause.
  - C. a due-on-sale clause.
  - D. a cooperation clause.
6. In an open listing, a broker receives a commission
  - A. by procuring the buyer.
  - B. by offering a co-op to other brokers in the MLS.
  - C. from anyone who sells the property.
  - D. only if the seller does not sell the property.
7. Which of these would be LEAST likely to appear in a listing contract?
  - A. Negotiable commission clause
  - B. Expiration date
  - C. Listing price
  - D. Estimated closing costs
8. A seller agrees to pay a broker a commission if the broker sells the seller's home. The seller makes the same agreement with three other brokers. This arrangement is MOST similar to which listing contract?
  - A. Exclusive right-to-sell
  - B. Exclusive agency
  - C. Open listing
  - D. Net listing
9. Listing brokerages are obligated to present all written offers to the seller
  - A. only if they are serious offers.
  - B. only if the buyer is preapproved for a mortgage.
  - C. promptly.
  - D. on a weekly basis.
10. Which of the following would NOT terminate a listing or buyer representation agreement?
  - A. Client or brokerage firm bankruptcy
  - B. Mutual agreement
  - C. Expiration of the contract
  - D. Client wishes to terminate
11. A buyer and a sales associate just signed a buyer's representation agreement. Who represents the buyer?
  - A. Sales associate's brokerage
  - B. Sales associate
  - C. Listing brokerage
  - D. Multiple listing service (MLS)

# UNIT 10 BROKER-LEVEL QUESTIONS

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1. A broker signed a six-month listing with a seller. The broker put a sign in the front yard and put the property in the MLS system. However, all of the other items the broker agreed to have not been completed, including the weekly open house that was agreed to in the listing contract. The seller
  - A. must wait until the end of the listing term to terminate.
  - B. may terminate the contract upon sending written notice of breach.
  - C. must give the broker 30 days' notice to produce or terminate.
  - D. will have to send a complaint to the state's real estate commission or other governing body to terminate the listing.

# UNIT 10 QUIZ ANSWERS

---

1. **B** The answer is to pay the broker a commission regardless of who procures the buyer. Under an exclusive right-to-sell listing, the broker is paid if the property sells, regardless of who found the buyer.
2. **D** The answer is death of the sales associate. Since the listing belongs to the brokerage and not the sales associate, the death of a sales associate does not terminate a listing. The death of the seller or the principal broker would terminate the contract.
3. **A** The answer is an exclusive agency listing. Under an exclusive agency listing, owners retain the right to sell the property on their own without compensating the listing broker.
4. **C** The answer is has promised to pay a commission if the property is sold during the listing period. In an exclusive right-to-sell listing, the broker is entitled to be paid if the property is sold during the listing period, regardless of who obtains the buyer.
5. **B** The answer is a protection or safety clause. This clause, which may be referred to as the protection, safety, extension, or holdover clause, protects the broker's commission for a period determined by state law.
6. **A** The answer is by procuring the buyer. The only broker paid in an open listing is the broker that finds (procures) a buyer. No commission will be paid if the property otherwise sells. A seller may enter into multiple open listings.
7. **D** The answer is estimated closing costs. Closing costs are estimated upon presentation of an offer, not in the listing contract.
8. **C** The answer is open listing. An open listing is one in which the seller may list with more than one brokerage, but only the broker who brings the buyer will get paid.
9. **C** The answer is promptly. The seller should receive all offers promptly and can determine the sincerity of all offers.
10. **D** The answer is client wishes to terminate. One party cannot terminate a contract—no unilateral rescission. However, if both parties can agree to terminate, it is a bilateral agreement.
11. **A** The answer is sales associate's brokerage. The sales associate signed the buyer representation agreement on behalf of the brokerage. Sales associates are employed by their brokerage as general agents, and are given a limited authority to bind the brokerage contractually.

## Broker-Level Questions

1. **B** The answer is may terminate the contract upon sending written notice of breach. The broker is in breach of contract and the seller, upon written notice, can terminate the listing.



# UNIT 11

## Real Estate Contracts

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the essential elements of a contract.
- › Explain the various means by which a contract may be enforced, terminated, assigned, or replaced.
- › Describe the primary written agreements and forms used in real estate sales and leasing.

### KEY POINTS—UNIT 11

- A contract is a legally binding document between two or more competent parties to do or not do certain things for consideration. An express contract has been put into words, either spoken or written. An implied contract is created by the actions of the parties.
- To comply with the statute of frauds (and be enforceable in court), all contracts for the sale or transfer of real estate must be express written contracts, with the exception of a lease for 12 months or less.
- A breach of contract occurs when a party fails, without legal excuse, to perform any promise contained in the contract. After a breach of contract, the nonbreaching party has four options: acceptance of partial performance, a lawsuit for specific performance, liquidated damages, or a suit for actual money damages.
- When a contract doesn't meet one or more of the requirements for a valid contract, it is considered legally void. If a contract appears to be valid, but has a defect that gives one or more of the parties the power to avoid performance and rescind the contract, it is a voidable contract.
- For a contract to be valid, the parties must have contractual capacity (be at least age 18 and mentally competent). There must also be mutual agreement between the parties, contractual intent, a lawful objective, and consideration, and the document must be in writing (for most real estate contracts).

- To create a valid contract, consent must be freely given. It is not freely given when it is the result of fraud, misrepresentation, duress, undue influence, or mistake. Under these conditions, the contract would be voidable by the disadvantaged party.
- An option contract is a unilateral contract. It creates a right for the optionee/buyer to buy or lease property for a fixed price during a limited time period. The optionor/seller must hold the property off the market and is obligated to sell if the option is exercised.
- The enforceability of contracts depends on the legal status of the document.

## I. CONTRACT LAW

- A contract is a voluntary, binding agreement between two or more competent parties to do (or not do) a specific thing.

### A. Implied contract

1. Actions indicate \_\_\_\_\_
2. No implied contracts in transfer of any interest in real estate

### B. Express (declared) contract

1. Express means \_\_\_\_\_
  - a. The state's statute of frauds requires most contracts dealing with real estate to be \_\_\_\_\_ to be enforceable.
  - b. To be enforceable, real estate contracts must be \_\_\_\_\_.
2. Bilateral contract
  - a. Promise exchanged for \_\_\_\_\_
  - b. Both parties are bound to perform.
  - c. Example: Purchase contract—"I promise to sell and you promise to buy."
3. Unilateral contract
  - a. Promise exchanged for \_\_\_\_\_
  - b. \_\_\_\_\_ is bound.
  - c. Example: Option contract—"I promise to sell if you decide to buy."
4. Executory vs. executed contracts
  - a. An \_\_\_\_\_ contract is created upon offer and communication of acceptance.
  - b. A purchase contract is considered \_\_\_\_\_ at closing upon delivery and acceptance of the deed.
5. Validity of a contract

**Figure 11.1: The Enforceability of Contracts**

Valid	<ul style="list-style-type: none"> <li>■ Binding and enforceable</li> <li>■ Contains all essential elements</li> </ul>	<ul style="list-style-type: none"> <li>■ A contract having all the requirements to be binding on the parties</li> </ul>
Void	<ul style="list-style-type: none"> <li>■ No contract at all</li> <li>■ Missing one or more essential elements</li> </ul>	<ul style="list-style-type: none"> <li>■ A contract for which there is no lawful objective</li> </ul>
Voidable	<ul style="list-style-type: none"> <li>■ Valid until rescinded by one party</li> </ul>	<ul style="list-style-type: none"> <li>■ A contract entered into by a minor or under duress or due to fraud or misrepresentation</li> </ul>

## a. Valid

- i. Meets all legal requirements; contains \_\_\_\_\_
- ii. Binding and enforceable in court by both parties

## b. Void

- i. No legal effect; not enforceable by either party
- ii. Lacks one or more of the essential elements of a valid contract, such as an oral contract for the purchase of real estate

## c. Voidable

- i. A voidable contract appears valid, but one party may disaffirm, such as when the party was subject to \_\_\_\_\_.
- ii. The disadvantaged party may take legal action to cancel the contract.

**II. CREATION OF A VALID CONTRACT (SEE FIGURE 11.2)****Figure 11.2: Essential Elements of a Real Estate Contract**

1. Competent parties
2. Mutual agreement
3. Lawful objective
4. Consideration
5. In writing and signed

**A. Contractual capacity/legally \_\_\_\_\_**

1. Must be \_\_\_\_\_ years old or an emancipated minor
2. Must be \_\_\_\_\_
  - a. Persons determined to be incompetent \_\_\_\_\_ cannot enter into a contract unless the court authorizes someone to act on their behalf.

**B. Mutual agreement—must have an \_\_\_\_\_**

1. Offer and communication of acceptance
  - a. A \_\_\_\_\_ becomes binding upon \_\_\_\_\_.
  - b. If the offer is withdrawn before communication of acceptance, there is no contract.
2. Counteroffer—any change to the conditions in the offer
  - a. A counteroffer \_\_\_\_\_.
  - b. In a counteroffer, the original offeree becomes an offeror.
  - c. If a seller made a counteroffer to a buyer and then received a new and better offer from a different buyer, the seller must withdraw the counteroffer before accepting the new offer.
  - d. An offeror/counterofferor may withdraw their offer at any time before acceptance, even if their offer allowed a specific period of time in which to accept.
  - e. A buyer who receives a counteroffer does not need to respond prior to writing an offer on a different property.
  - f. A seller who makes changes to the offer document, then initials and signs the offer, has created a counteroffer.
3. Contractual intent
  - a. Intent to be bound
4. No fraud or misrepresentation
  - a. The parties may not make false statements or \_\_\_\_\_.
  - b. Making a claim that anyone would construe as not literally true, known as \_\_\_\_\_, is not misrepresentation.
  - c. An agent may rely on a seller's statement of repair unless it is apparent that it is not true.
  - d. Sellers and agents must disclose all material defects and facts, even if selling "as is."
    - i. "As is" means the seller will not fix anything.
5. No duress or menace
  - a. No force or threat
6. No undue influence
  - a. No unfair advantage



**C. Lawful objective**

1. The contract must have a legal purpose.
2. The contract would become void if the use of the property was banned during the contract period.

**D. \_\_\_\_\_**

1. Consideration is money, promises, or something of value.
2. It is customary, but not essential, for a purchaser to provide a deposit called \_\_\_\_\_.

**E. In writing and signed****III. CONTRACTS USED IN THE REAL ESTATE BUSINESS****A. Use of contract forms**

1. Practice of \_\_\_\_\_ includes preparation of legal documents.
2. Many states permit \_\_\_\_\_ to assist clients and customers in completing preprinted forms.

**B. Sales contract**

1. Contains complete agreement between seller of real estate and buyer
2. Also known as offer to purchase, contract of purchase and sale, purchase agreement, earnest money agreement, or deposit receipt
3. The offer becomes an \_\_\_\_\_ contract upon communication of acceptance.
  - a. Communication of acceptance occurs when the last party has signed and the other party has been notified.
  - b. Method of communication is determined by the contract or state law.
4. Bilateral contract: binding on both parties
  - a. Seller promises to \_\_\_\_\_.
  - b. Buyer promises to \_\_\_\_\_.
5. Essential elements include being in writing and signed by the buyer and seller, property description, price, and terms.

6. Typically includes one or more \_\_\_\_\_ stating that the party will not be obligated to complete the purchase under certain conditions.
  - a. Typical contingencies include financing and inspection.
  - b. If the buyer terminates per a contingency, \_\_\_\_\_ and the contract is terminated.
  - c. Brokerage is not entitled to a commission if the contract is terminated per a contingency.
7. Contracts often include a “time is of the essence” clause, which requires exact adherence to dates specified in the contract.
8. A risk of loss statement is determined by state law or contract provision.

### C. Option

1. Definition: A buyer purchases the right to buy at a \_\_\_\_\_.
2. Parties
  - a. Owner—optionor
  - b. Potential buyer—optionee
3. Unilateral contract: “I promise to sell if you decide to buy.”
  - a. Binding on seller: Buyer has choice to perform.
  - b. Original contract contains all terms that will become binding if the option is exercised.
  - c. Becomes bilateral when exercised by the optionee
  - d. If the option is not exercised, it expires at the end of the option period.
4. Option fee
  - a. Typically includes a nonrefundable option fee
    - i. The parties negotiate whether the option fee will be applied toward the purchase price.
  - b. If the buyer decides not to buy, the seller has no recourse except to keep the buyer’s option fee.

### D. Owner financing contracts

1. Seller provides credit for all or part of the purchase funds.
2. Seller retains legal title under what is commonly known as a \_\_\_\_\_.
3. Buyer has \_\_\_\_\_ until sufficient payments have been made, possibly according to state law.
4. Seller who finances a sale can use a \_\_\_\_\_ that places title in the buyer but gives the seller a security interest in the property.

#### IV. OTHER FEATURES OF A CONTRACT

##### A. Addendum

1. Additional material attached to and made \_\_\_\_\_ (e.g., disclosures and contingencies)

##### B. Amendments/modification

1. \_\_\_\_\_ of an existing contract by mutual agreement
2. Must be \_\_\_\_\_ by all parties

##### C. Assignment

1. Transfers \_\_\_\_\_, but not liability

##### D. Novation

1. Transfers contract rights and liability
2. \_\_\_\_\_.

#### V. TERMINATION OF CONTRACTS

##### A. Legal impossibility/impossibility of performance

1. A duty required by the contract that cannot be legally performed means that the contract becomes \_\_\_\_\_.

##### B. Contingency

1. The contract is terminated if a contingency cannot be met.
2. The buyer's \_\_\_\_\_ is returned.

##### C. Mutual rescission

1. All parties agree to cancel the contract (earnest money is typically \_\_\_\_\_).

##### D. Death

1. Most contracts are not terminated by death.
  - a. The deceased's estate must honor the contract.
  - b. Contract would terminate if there are no heirs/devisees to perform.
2. Certain contracts may be terminated by death, such as the death of the broker in a representation agreement, which is a personal services contract.
3. Offers, which are not contracts, terminate upon death of the parties.

## VI. REMEDIES FOR BREACH/DEFAULT OF CONTRACT

### A. How a breach of contract occurs

1. A breach of contract occurs when one party is in default.
  - a. Example: A seller removes fixtures that were not excluded from the purchase contract.
  - b. Example: A buyer's earnest money check is returned for nonsufficient funds.
  - c. The \_\_\_\_\_ sets forth the amount of time in which legal action may be taken against the breaching party.

### B. Remedies for the nonbreaching party

1. Acceptance of partial performance
  - a. \_\_\_\_\_
2. Specific performance
  - a. Sue to force performance—\_\_\_\_\_
  - b. Available to \_\_\_\_\_ buyer and seller
  - c. Buyer's only remedy if the seller decides not to sell
3. Liquidated damages (available only if specified in the contract)
  - a. Retain breaching party's earnest money deposit
  - b. Available \_\_\_\_\_ in a purchase contract
4. Actual damages
  - a. Sue for \_\_\_\_\_

## UNIT 11 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

addendum	express	offeree
amendment	fraud	offeror
bilateral	implied	option
communication of acceptance	land contract	specific performance
consideration	lawful objective	statute of frauds
contingency	lease	unilateral
counteroffer	legal	valid
earnest money	liquidated damages	void
executory	mutual agreement	voidable

1. A contract with terms that have been explicitly declared either verbally or in writing is a(n) \_\_\_\_\_ contract.
2. When only one party to the contract makes a promise, the result is a(n) \_\_\_\_\_ contract.
3. A contract in which one party has the right to cancel the contract because they were subject to fraud, duress, or misrepresentation is a(n) \_\_\_\_\_ contract.
4. A contract created by the actions of the parties is a(n) \_\_\_\_\_ contract.
5. A real estate purchase in which the buyer does not immediately receive full legal title to the property is a \_\_\_\_\_.
6. The provision in a contract that allows buyers to cancel and have their earnest money refunded if they cannot qualify for a loan is known as a(n) \_\_\_\_\_.
7. A unilateral contract in which the buyer has the right to purchase a property from the seller at an agreed-on price for a set time period, but only if the buyer chooses to do so, is a(n) \_\_\_\_\_.
8. A party attempting to enforce an oral executory contract for the purchase of real estate would be stopped by the \_\_\_\_\_.
9. \_\_\_\_\_ means that there was an offer and communication of acceptance; there was no fraud, misrepresentation, or mistake; and the consent was genuinely and freely given.
10. The party who makes an offer to another is known as the \_\_\_\_\_.
11. An accepted offer becomes binding upon \_\_\_\_\_.
12. Entering into a contract by intentionally deceiving a party is \_\_\_\_\_.
13. Something of value given in exchange for something else of value is \_\_\_\_\_.
14. \_\_\_\_\_ is often included in an offer as liquidated damages to the seller, should the buyer breach the purchase contract.
15. Additional material attached to and made part of an offer is a(n) \_\_\_\_\_.
16. To modify a written contract, both parties must sign a(n) \_\_\_\_\_.
17. The buyer has equitable title in a(n) \_\_\_\_\_ contract, while the seller retains \_\_\_\_\_ title.
18. The right of parties to a contract to sue each other to perform according to the terms of the contract is \_\_\_\_\_.
19. When the seller keeps only the earnest money deposit of a buyer who is in default, the contract remedy is \_\_\_\_\_.

## UNIT 11 GLOSSARY REVIEW ANSWERS

1. express
2. unilateral
3. voidable
4. implied
5. land contract
6. contingency
7. option
8. statute of frauds
9. Mutual agreement
10. offeror
11. communication of acceptance
12. fraud
13. consideration
14. Earnest money
15. addendum
16. amendment
17. executory, legal
18. specific performance
19. liquidated damages

# UNIT 11 QUIZ

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1. A contract that has NOT yet been fully performed is
  - A. unenforceable.
  - B. voidable.
  - C. executory.
  - D. executed.
2. A contract that exchanges a promise for performance is
  - A. implied.
  - B. unilateral.
  - C. bilateral.
  - D. executory.
3. All of these are essential elements of a contract EXCEPT
  - A. mutual agreement.
  - B. a lawful objective.
  - C. consideration.
  - D. earnest money.
4. The electrical wiring in a house is defective. The broker who listed the house is aware of this and intentionally deceives a potential buyer about it. The buyer purchases the home and later suffers a financial loss as a result of the faulty wiring. This is an example of
  - A. mistake of law.
  - B. fraud.
  - C. mistake of fact.
  - D. novation.
5. Which of the following requires real estate sales contracts to be in writing?
  - A. Caveat emptor law
  - B. Truth in Lending Act
  - C. Statute of limitations
  - D. Statute of frauds
6. Which of the following statements regarding a purchase contract is TRUE?
  - A. The contract is binding on both parties.
  - B. The contract may be oral.
  - C. The contract terms must be identical to the terms in the listing contract.
  - D. The contract conveys legal title when signed by both parties.
7. A new contract that transfers all rights and liabilities is
  - A. an assignment.
  - B. a subordination.
  - C. a novation.
  - D. an option.
8. A seller may keep the buyer's earnest money as liquidated damages if
  - A. that is stated in the listing contract as a remedy for the seller.
  - B. the seller and the broker agree that the buyer defaulted and the contract calls for specific performance.
  - C. the buyer defaults and the purchase contract stipulates liquidated damages as a remedy.
  - D. the seller failed to perform an essential element of the contract.
9. A contract in which one party purchases the right to buy at a fixed price within a specified period is
  - A. a purchase contract.
  - B. a listing contract.
  - C. a lease.
  - D. an option.
10. A contract between two parties that legally binds one party to perform, but allows the other party to disaffirm it, is
  - A. executed.
  - B. void.
  - C. voidable.
  - D. bilateral.
11. A buyer and seller signed a purchase contract, but then the seller refused to sell. The buyer sued the seller successfully and was able to purchase the house. What was the contract remedy?
  - A. Unilateral rescission
  - B. Mutual agreement
  - C. Specific performance
  - D. Damages

12. When a party is in default in a contract because of a missed payment deadline, the contract is considered
  - A. breached.
  - B. executed.
  - C. unilateral.
  - D. illegal.
13. Upon acceptance and then communication of acceptance, an offer is considered
  - A. a counteroffer.
  - B. unilateral.
  - C. a binding contract.
  - D. valid.
14. The buyer and the seller have entered into a binding contract for sale. However, before closing, the law changes and the buyer's intended use of the property becomes illegal. This means the contract is
  - A. valid and enforceable under the rules of risk.
  - B. terminated because of fraud by the seller.
  - C. void due to impossibility of performance.
  - D. valid, but the price must be renegotiated.
15. When the buyer is in default and the seller keeps the earnest money, the contract MOST likely provided for
  - A. specific performance.
  - B. actual damages.
  - C. executed damages.
  - D. liquidated damages.
16. A remedy for parties in default that is available to both the buyer and the seller in a purchase contract is
  - A. specific performance.
  - B. liquidated damages.
  - C. actual damages.
  - D. lis pendens.
17. The seller told the buyer that the property had no roof leaks. However, when the buyer had the property inspected, a roofing contractor found leaks, and said the roof had been leaking for months. The contract between the seller and the buyer is MOST likely
  - A. void.
  - B. voidable.
  - C. valid.
  - D. implied.
18. Contracts that transfer interests in real estate should be
  - A. implied contracts.
  - B. unilateral contracts.
  - C. bilateral contracts.
  - D. express written contracts.
19. A contract between two parties who each make a promise to perform certain acts is called
  - A. a bilateral contract.
  - B. a unilateral contract.
  - C. an implied contract.
  - D. a voidable contract.
20. A purchase contract would likely be voidable under all of these circumstances EXCEPT
  - A. the purchaser has a legal guardian of their financial affairs who is unaware of the contract.
  - B. the seller signed under duress.
  - C. the buyer didn't read or understand the contract.
  - D. the seller made a material misrepresentation to the buyer.
21. An offer to purchase includes a clause stating the contract will be canceled and earnest money will be returned to the buyer if the buyer cannot obtain financing. The clause is
  - A. an option.
  - B. voidable.
  - C. equitable title.
  - D. a contingency.
22. A buyer is unable to obtain financing and terminates a contract as allowed by the financing contingency. Which of the following is FALSE?
  - A. The brokerage is entitled to a commission.
  - B. Earnest money will be refunded to the buyer.
  - C. The seller has no legal recourse against the buyer.
  - D. The contract is terminated.



# UNIT 11 BROKER-LEVEL QUESTIONS

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1. Pam approaches her neighbor, Bob, after seeing his For Sale by Owner (FSBO) sign, and asks about the price and what is being offered. Pam and Bob write on a piece of notebook paper what they agree to for the sale. There are several items scratched out and rewritten, but after they finalize the agreement, they both sign it. What type of agreement do they have?
  - A. Nothing, because purchase contracts must be written on approved forms
  - B. A counteroffer, which terminated the original offer when they crossed out items
  - C. Pam has an option until the agreement is put into an approved real estate contract form
  - D. An expressed executory contract for the purchase and sale of the property
2. After weeks of negotiation, a buyer and a seller finally have an executory contract for the purchase of a hair salon business. All of the contingencies have been met a week before the closing, but then the seller discovers there has been a change in the zoning, which will no longer allow the property to be used as a hair salon. The contract is now
  - A. void.
  - B. valid.
  - C. voidable by the buyer.
  - D. voidable by the seller.
3. A buyer and a seller are under contract for the purchase of a home. At the inspection, the buyer finds numerous small issues that need to be addressed. The seller arrives home at the end of the inspection and reviews the list with the buyer. The seller agrees verbally to complete the items on the list. At the walk-through on the day of closing, the buyer finds that none of the items have been corrected. In this case, what will occur?
  - A. The seller will have to give the buyer funds at closing to cover the work that was agreed to.
  - B. The buyer should send notice to terminate unless the work is done.
  - C. The contract will automatically be extended a week to allow the seller to complete the work.
  - D. The buyer may have to sue the seller to complete the work or provide funds for the buyer to complete the work.
4. Which of these BEST describes the primary purpose of a real estate purchase contract?
  - A. To create the conditions and terms for closing
  - B. To set up the seller's right to liquidated damages
  - C. To allow the seller to have equitable title
  - D. To establish how the real estate brokerage will be paid
5. Two buyers are under contract to buy a home from an older married couple. Two weeks after contract acceptance, the buyer's broker hears that one of the sellers has died. This means the contract is
  - A. terminated, with the living spouse keeping the earnest money.
  - B. valid until there is no one able to perform.
  - C. void because it was signed by both parties.
  - D. valid only if title was held as joint tenants.

# UNIT 11 QUIZ ANSWERS

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1. **C** The answer is executory. Before execution, the contract is executory.
2. **B** The answer is unilateral. A promise for a promise is bilateral; a promise for performance is unilateral.
3. **D** The answer is earnest money. Earnest money is not an essential element of a contract. Earnest money typically is used as liquidated damages for the seller to retain in the event of the buyer's breach.
4. **B** The answer is fraud. Intentional deceit is fraud.
5. **D** The answer is statute of frauds. The statute of frauds requires all real estate contracts (except leases for one year or less) to be in writing.
6. **A** The answer is the contract is binding on both parties. A purchase contract is binding on both the buyer and the seller.
7. **C** The answer is a novation. A transfer of contract rights and liabilities to another using a new contract is a novation.
8. **C** The answer is the buyer defaults and the purchase contract stipulates liquidated damages as a remedy. If the buyer breaches the purchase contract, the seller may keep the earnest money as liquidated damages if the purchase contract provides for that remedy.
9. **D** The answer is an option. In an option, the optionee purchases the right to buy.
10. **C** The answer is voidable. In most voidable contracts, only one of the parties is legally bound to perform.
11. **C** The answer is specific performance. An order of specific performance requires the defaulting party to perform as agreed in the contract.
12. **A** The answer is breached. A party who is in default in a contract is said to be in breach of contract.
13. **C** The answer is a binding contract. Upon communication of acceptance, the offer becomes a binding contract.
14. **C** The answer is void due to impossibility of performance. When a change in law makes the purpose of a contract illegal, it is void due to impossibility of performance (it now lacks a legal purpose).
15. **D** The answer is liquidated damages. The buyer agrees to provide an earnest money deposit to the seller in case the buyer defaults on the contract. It is typically the only damages the seller will receive in a liquidated damages contract.
16. **A** The answer is specific performance. Specific performance is the only standard remedy for default that is available to both parties in a purchase contract.
17. **B** The answer is voidable. The contract is voidable because of the fraudulent misrepresentation of the condition of the property.
18. **D** The answer is express written contracts. Express (meaning that the terms are specifically identified in the contract) written contracts are used in the transfer of real estate.
19. **A** The answer is a bilateral contract. A bilateral contract contains a promise from each party.
20. **C** The answer is the buyer didn't read or understand the contract. Failure to read the contract does not allow a party to withdraw.
21. **D** The answer is a contingency. Contingency clauses in a contract state that a party will not be obligated to complete the purchase under agreed-on circumstances, typically involving financing and inspection.
22. **A** The answer is the brokerage is entitled to a commission. The brokerage is not entitled to a commission if a contract is terminated per a contingency.

**Broker-Level Questions**

1. **D** The answer is an expressed executory contract for the purchase and sale of the property. Pam and Bob created an express written contract for the sale. They could choose to put the agreement in a standard contract form, but it is not required.
2. **A** The answer is void. The contract now lacks a lawful objective, so it is void.
3. **D** The answer is the buyer may have to sue the seller to complete the work or provide funds for the buyer to complete the work. Because there is no written agreement for the work to be completed, the buyer will need to sue the seller to complete the work. It is a real estate professional's obligation to put such agreements in writing so the parties know what is expected.
4. **A** The answer is to create the conditions and terms for closing. The main purpose of the real estate purchase contract is to set up the conditions and terms for closing. It may also establish default remedies, but that is not the main purpose. The seller retains legal title, and commissions are not typically noted in a purchase contract.
5. **B** The answer is valid until there is no one able to perform. The contract is valid and will remain so until there is no one left to perform. The buyers would most likely ask what the surviving spouse wants to do and would allow the contract to be terminated if the spouse chose to keep the property. However, this is not a requirement of contract law.



# UNIT 12

## Real Estate Financing

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the factors that contribute to housing affordability, including interest rates and ability to pay.
- › Describe the terms, conditions, and use of the promissory note.
- › Explain the elements and use of the mortgage and deed of trust, and the roles of the parties involved in each.
- › Describe the various types of real estate financing.
- › Explain the distinction between a judicial foreclosure and a nonjudicial foreclosure, and the process involved in each.
- › Describe the various consumer protections related to homeownership.

### KEY POINTS—UNIT 12

- A promissory note is a written promise to repay a debt. A promissory note for a real estate loan is almost always accompanied by a mortgage or deed of trust on the property, either of which creates a lien against the property, allowing the lender to foreclose in case the loan is not paid as promised.
- When a mortgage is paid in full, a satisfaction of mortgage is used to release the mortgage lien. A reconveyance deed is used to release a deed of trust.
- The loan-to-value ratio (LTV) is what a lender uses to determine the maximum loan amount for a transaction. The LTV is based on the appraised value or sales price of the property, whichever is less.
- A lender charges discount points to increase the yield on the loan. The points are paid at closing by either the buyer or the seller. One point is 1% of the loan amount.
- Equity is the difference between the value of a property today and the debt against the property today.

- Most foreclosure laws are created at the state level, but they all share some common concepts. The lender files a notice of default, and then the borrower is given a time period to repay the debt and redeem the property. If the borrower cannot clear the default, the property goes to sale. The sale removes all liens against the property. The winner of the bid then has the right, based on state laws, to obtain title to the property.
- A straight note or term note is a loan in which interest-only payments are made during the term, with the full amount of the principal due at the end in a balloon payment. With a partially amortized loan, payments include both principal and interest and there will be a balloon at the end. If a note is fully amortized, the entire principal amount and all of the interest will be paid off within the agreed loan period.
- With a fully amortized loan, the interest rate and the amount of the payment remain the same throughout the term of the loan. But there are various alternative repayment plans, such as adjustable-rate mortgages (ARMs).
- Leverage is using borrowed money to purchase real estate. The higher the debt, the higher the leverage, the higher the risk of default, and the lower the down payment.

## I. HOUSING AFFORDABILITY

### A. Buy vs. rent decision factors

1. How long a person wants to live in a particular area
2. The person's financial situation
3. Housing affordability, directly affected by
  - a. Supply of housing
  - b. Current mortgage interest rates
4. Tax consequences of owning versus renting property
5. Anticipation of future home values and tax rates

### B. Mortgage terms

1. Competitive interest rates are offered on conventional loans.
2. Federal Housing Administration (FHA) and U.S. Department of Veterans Affairs (VA) have programs with \_\_\_\_\_ and lower credit score requirements.

### C. Ownership expenses and ability to pay

1. Basic costs of home ownership are referred to as PITI and include \_\_\_\_\_.
2. A lender will look at a consumer's \_\_\_\_\_ as compiled by a credit reporting company.
3. Fair Isaac and Company developed the \_\_\_\_\_.

4. Lenders also look at a loan applicant's DTI, or percentage of \_\_\_\_\_.
5. Lenders also consider a loan applicant's LTV, which is the \_\_\_\_\_.

## II. PROMISSORY NOTE

### A. The promissory note is also called the financing instrument.

1. The promissory note is a legal instrument that provides \_\_\_\_\_.
  - a. Secured by the mortgage
  - b. Held by the lender until the loan is fully repaid; not recorded
2. Key elements
  - a. Personal promise of the borrower to repay a fixed amount
  - b. Terms of repayment
  - c. Signature of the borrower; the lender does not sign
3. Special provisions
  - a. Acceleration clause
    - i. If the borrower \_\_\_\_\_, the lender can demand immediate payment of the \_\_\_\_\_.
  - b. The promissory note alone does not create a lien on the property.
  - c. Most real estate notes are negotiable and transferable, which allows them to be sold.

### B. Interest

1. Charge for the use of money, expressed as a percentage of the \_\_\_\_\_
2. Usually, loan payments are made at the end of a period, or \_\_\_\_\_.
3. Loan payments also could be paid \_\_\_\_\_.

### C. Usury

1. Charging interest in excess of the maximum rate allowed by law is called \_\_\_\_\_.
2. State law may limit the interest rate that may be charged on loans.
3. Federal law \_\_\_\_\_ federally related residential first mortgage loans from state usury laws.

**D. Loan origination fee**

1. Also called a \_\_\_\_\_
2. Covers lender's expenses on originating the loan
3. Typically, about \_\_\_\_\_ of the loan amount

**E. Discount points**

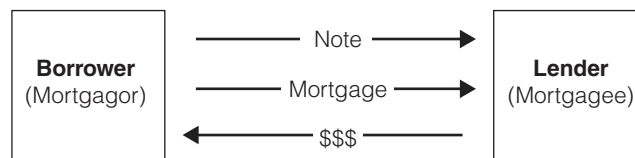
1. Increase lender's yield (rate of return) on loaned money
2. One discount point equals \_\_\_\_\_ of the loan amount.

**F. Prepayment penalty**

1. Provides an extra payment to the lender if a loan is paid off in its early years

**III. SECURITY INSTRUMENT****A. Mortgage or deed of trust (security instruments)**

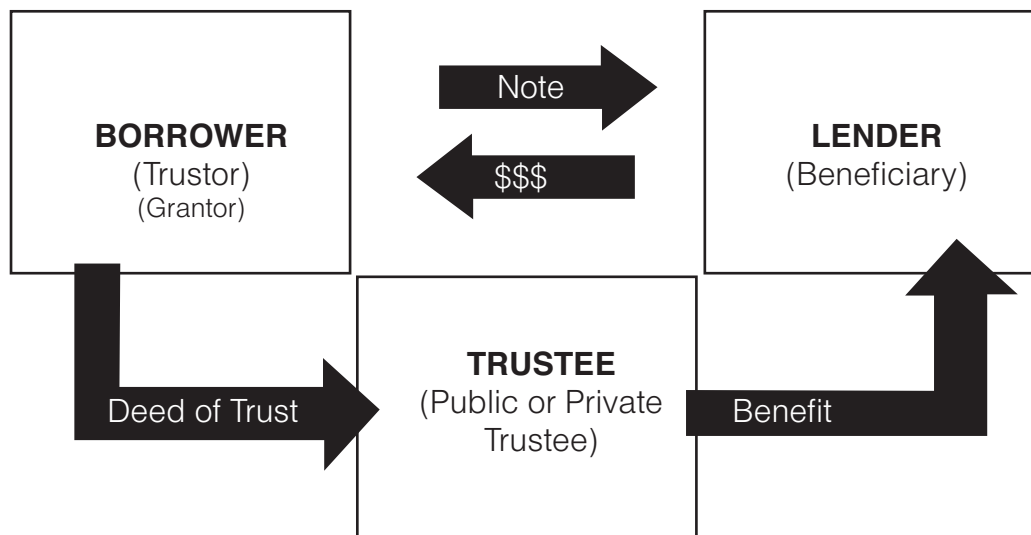
1. Instruments that pledge (hypothecate) property as security for a debt
2. Mortgage or deed of trust creates a lien when recorded.
  - a. Creates payment obligation to pay off principal and interest
  - b. Interest on the majority of a home loan is \_\_\_\_\_, not compounded.
3. Allows for foreclosure if borrower defaults on the note
4. Mortgage: two-party instrument
  - a. The borrower is the \_\_\_\_\_ who gives a mortgage to the lender.
  - b. The lender is the \_\_\_\_\_ (see Figure 12.1).

**Figure 12.1: Mortgage**



5. Deed of trust: three-party instrument (see Figure 12.2)
  - a. The borrower is the trustor.
  - b. The lender is the \_\_\_\_\_ (benefits from the trust).
  - c. Trustee—in some states, a public official
6. Like all contracts, a mortgage requires the essential elements and must be in writing and signed to be valid.

**Figure 12.2: Deed of Trust**



### **B. Provisions of a mortgage/deed of trust**

1. Defines the rights and obligations
2. Acceleration clause—The lender may demand full payment in case of default.
3. Defeasance clause—When debt is paid (mortgage/deed of trust), the lien must be removed.
  - a. The mortgagee provides “satisfaction.”
  - b. The trustee provides the deed of reconveyance.
  - c. Satisfaction or reconveyance deed proves payments are in full and are recorded by the borrower.
4. \_\_\_\_\_—also called an alienation clause
  - a. Provides that when the property is \_\_\_\_\_, the lender may demand immediate payment of the outstanding debt
  - b. Lender consent is required for assumption of a loan.

5. Prepayment clause—establishes terms and conditions for early loan payoff.
  - a. May include penalties for early payoff (prepayment penalty)
6. Power of sale clause—optional provision in mortgage if allowed by state law; standard in deeds of trust
  - a. Gives the trustee/mortgagee the power to foreclose without going to court (nonjudicial)

### **C. Reasons for loan acceleration and foreclosure**

1. Nonpayment of principal and interest
2. Nonpayment of taxes
3. Removal of improvements without lender's permission
4. Insurance coverage lapse
5. \_\_\_\_\_—would include deferred maintenance that lowers value below what is owed.
6. Alienation without consent (if there is a due-on-sale clause)

## **IV. MISCELLANEOUS MORTGAGE TERMS**

### **A. Leverage**

1. Use of borrowed money to finance a purchase
  - a. The higher the LTV (the more money borrowed), the higher the leverage.
  - b. The disadvantage of high leverage is the greater risk of default (lower equity equals higher risk).
  - c. The advantage of leverage is the ability to control a large asset with a relatively small cash investment.

### **B. Subordination**

1. A clause in a mortgage/deed of trust that allows a subsequent mortgage to \_\_\_\_\_
  - a. The subordinate mortgage will maintain its \_\_\_\_\_.
2. If a previous first mortgage/deed of trust is refinanced, the second mortgage/deed of trust continues in its second position.

**V. FORECLOSURE—GOVERNED BY STATE LAWS****A. Key points**

1. Foreclosure is a procedure whereby property used as security for a debt is taken by a creditor/lender and \_\_\_\_\_.
- a. The foreclosure process removes \_\_\_\_\_ from the property.
2. The types of foreclosures include the following:
  - a. Foreclosure by judicial (legal) action
  - b. Nonjudicial foreclosure

**B. Judicial foreclosure**

1. Lawsuit to obtain the power to foreclose from a court
2. Lis pendens is filed with county recorder.

**C. Nonjudicial foreclosure**

1. Trustees and mortgagees have the right to foreclose without going to court.
2. The mortgage or deed of trust must have a power of sale clause.

**D. Strict foreclosure**

1. Notice is given to the delinquent borrower.
2. The court sets a deadline for the balance of the \_\_\_\_\_ to be paid in full.
3. If the debt remains unpaid, the court awards full legal title of the property to \_\_\_\_\_.
4. No sale takes place.

**E. Deed in lieu of foreclosure (alternative to foreclosure)**

1. The borrower deeds the property to the lender to avoid foreclosure.
2. Sometimes known as \_\_\_\_\_
3. The lender takes title subject to any remaining liens.
4. The lender may not be willing to accept an encumbered title.

**F. Redemption**

1. Foreclosure sale
  - a. The lender sends a demand to foreclose.
  - b. The property is sold to the highest bidder at public auction.
  - c. The lender is often the sole bidder.
2. Equitable redemption period: right to stop foreclosure
  - a. The borrower cures by paying \_\_\_\_\_, plus interest and penalties.
  - b. The time period from when the lender declares default until the sale is determined by state law
3. Sale date starts the statutory redemption period
  - a. The borrower must pay full principal plus interest and fees to redeem.
  - b. At the end of the statutory redemption period, the highest bidder receives a deed to the property.
4. Lenders sell real estate owned (REO) property after the statutory redemption period to satisfy the debt.
  - a. Excess sale proceeds belong to the borrower.
  - b. Insufficient sale proceeds may result in a \_\_\_\_\_ judgment against the borrower.

**G. Deficiency judgment**

1. Foreclosure sale proceeds do not cover amount owed.
2. Deficiency judgment is a personal judgment against the debtor for any remaining amount owed.
3. Some states prohibit a deficiency judgment when the property is the debtor's principal residence.

**H. Short sale**

1. The borrower attempts to sell an "upside down" property.
  - a. Market value is less than the debt on the property.
2. A brokerage lists the property for sale at current market value.
3. Once an offer is accepted, the lender may or may not agree to accept the reduced (deficient) price.
4. Depending on state law, the lender may require the seller to pay any deficiency.
5. If part of the debt is forgiven, the seller may have tax consequences.

## VI. TYPES OF LOANS

### A. Term (straight) loan

1. \_\_\_\_\_ payments until maturity or at end of term
2. Entire principal paid back in a lump sum— \_\_\_\_\_ payment

### B. Partially amortized (balloon) loan

1. Equal payments of principal and interest
2. Lump-sum balloon payment at end of loan term

### C. Fully amortized loan—fixed rate

1. Equal consecutive installments of principal and interest
2. Balance decreases with each payment
3. Balance becomes zero at maturity

### D. Adjustable-rate mortgage (ARM)

1. The interest rate is subject to change based on an \_\_\_\_\_ or indicator.
2.  $\text{Index} + \text{margin} = \text{new rate}$
3. May include annual adjustment caps and/or lifetime rate caps
4. An appropriate loan for short-term owners
5. Not recommended for borrowers on a fixed income, such as a \_\_\_\_\_

### E. Growing equity mortgage

1. Also called a \_\_\_\_\_
2. The interest rate is fixed, but payments of principal are increased per an index or schedule.
3. The loan is paid off more quickly.
4. Most frequently used when the borrower's income is expected to grow to keep pace with increasing loan payments

**F. Balloon payment loan**

1. Periodic payments on a loan are not enough to fully pay off the principal, resulting in a final payment that is larger than the others.
2. State law defines a balloon payment, which typically is \_\_\_\_\_ the size or more of earlier payments.
3. The lender may agree to extend the term of the loan when the balloon payment is due.

**G. Reverse mortgage**

1. For seniors \_\_\_\_\_
2. The borrower receives a lump sum, monthly advances, or a credit line from the lender.
3. Allows the borrower to access equity in the home without selling it
4. The amount borrowed is repaid upon the death of mortgagor, upon the sale of the property, or when the property is no longer the senior's place of residence.

**H. Other mortgage features**

1. Package mortgage
  - a. Includes real property plus personal property
  - b. Example: a furnished condominium
2. Blanket mortgage
  - a. Typically used by developers
  - b. A \_\_\_\_\_ with more than \_\_\_\_\_ used as security
  - c. A partial release clause allows individual parcels to be released from lien as the balance is paid down.
3. Construction mortgage
  - a. Interim financing is made available in installments (draws) as improvements are completed
  - b. Typically adjustable-rate/short-term loans
  - c. The lender may require a "take-out" loan commitment if the builder intends to hold the property.
4. Home equity loans
  - a. The owner borrows against the equity in the home.
  - b. A home equity loan is paid out in a lump sum.

5. Home equity line of credit (HELOC)
  - a. The borrower receives access to the full loan amount.
  - b. Similar to a credit card—the debt is secured by the home equity.
  - c. Advances are limited to the difference between the approved loan amount and the current balance owed.

## **VII. CONSUMER PROTECTIONS**

### **A. Dodd-Frank**

1. The Consumer Financial Protection Bureau (CFPB) requires a consumer information pamphlet be provided by the \_\_\_\_\_.
2. More information about loan processing must be provided.
3. Consumer complaints must be resolved quickly.

### **B. Homeowners insurance**

1. A benefit to the homeowner that will be required by a lender
2. Basic form homeowners insurance covers losses caused by most frequently occurring natural disasters, theft, vandalism, and other hazards.
3. \_\_\_\_\_ homeowners insurance includes falling objects, building collapse, appliance-caused damages, and electrical damage.
4. The Comprehensive Loss Underwriting Exchange (CLUE) is a database of \_\_\_\_\_.

### **C. National Flood Insurance Program**

1. Created to provide insurance for property owners in flood prone areas
2. Administered by the Federal Emergency Management Agency (FEMA)
3. In special flood hazard areas, flood insurance is required on \_\_\_\_\_.

## UNIT 12 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

acceleration clause	equitable redemption	purchase money mortgage
adjustable-rate mortgage (ARM) loan	equity	reverse mortgage
alienation clause	fully amortized loan	security
balloon	leverage	statutory redemption
blanket mortgage	mortgage amount	term loan
contract for deed	package mortgage	
	partially amortized loan	

- The borrower's right to cure the default and stop the foreclosure sale is \_\_\_\_\_.
- A(n) \_\_\_\_\_ would not be recommended for a retiree on a fixed income.
- The clause that appears in both the note and the mortgage that allows the lender to demand immediate payment of the entire debt if the borrower defaults is a(n) \_\_\_\_\_.
- A loan that is repaid in one single lump sum at the end of its life is called a straight loan or \_\_\_\_\_.
- A loan in which payments are scheduled so the entire principal balance is repaid by the maturity date is a(n) \_\_\_\_\_.
- Term loans and partially amortized loans have a final \_\_\_\_\_ payment that is larger than the monthly payments and used to repay the remaining loan balance.
- A(n) \_\_\_\_\_ is used when more than one property is pledged as security for a single loan.
- A mortgage given by the purchaser to the seller in partial payment for the property is a(n) \_\_\_\_\_.
- The difference between a property's market value and the debts against it is \_\_\_\_\_.
- A loan that allows a borrower to make smaller payments of interest and principal but has a balloon payment at the end is a(n) \_\_\_\_\_.
- If a borrower sells the property and the buyer starts making payments on the loan without permission of the lender, the clause that allows the lender to call the loan due and payable is the \_\_\_\_\_.
- Points charged by lenders are computed as a percentage of the \_\_\_\_\_.
- The higher the LTV, the higher the \_\_\_\_\_.
- The mortgagee makes payments to the mortgagor in a \_\_\_\_\_.
- A mortgage or deed of trust provides a lender with \_\_\_\_\_ for the promissory note, pledging the real estate property as collateral for the debt.



## UNIT 12 GLOSSARY REVIEW ANSWERS

1. equitable redemption
2. adjustable-rate mortgage (ARM) loan
3. acceleration clause
4. term loan
5. fully amortized loan
6. balloon
7. blanket mortgage
8. purchase money mortgage
9. equity
10. partially amortized loan
11. alienation clause
12. mortgage amount
13. leverage
14. reverse mortgage
15. security

# UNIT 12 QUIZ

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1. Which of these terms are closest in meaning?
  - A. Mortgagor, lender
  - B. Mortgagee, borrower
  - C. Lender, mortgagee
  - D. Borrower, lender
2. An instrument used to pledge real property as security for a loan is
  - A. a bill of sale.
  - B. a chattel agreement.
  - C. a promissory note.
  - D. a mortgage.
3. The right of the borrower to reclaim the property before the foreclosure sale is
  - A. the right of first refusal.
  - B. the equitable redemption.
  - C. the riparian right.
  - D. the statutory right of redemption.
4. Principal is defined as
  - A. the total amount paid to the lender over the life of the loan.
  - B. the portion of each payment that is first applied to monthly payments.
  - C. the total interest paid over the life of the loan.
  - D. the original loan amount.
5. Which statement BEST describes a blanket loan?
  - A. More than one property is pledged as security for the loan.
  - B. Prepayment penalty for selling early
  - C. Covers both real and personal property
  - D. Ability to have several loans at one time
6. Owners' equity in their property is BEST described as
  - A. the difference between the current market value and the amount owed.
  - B. the difference between the original purchase price and the amount owed.
  - C. the current market value of the property.
  - D. the total outstanding debt against the property.
7. The disadvantage of being highly leveraged is that
  - A. more down payment will be required.
  - B. borrowers have more equity.
  - C. borrowers are more likely to default.
  - D. there are lower monthly payments.
8. The clause appearing in both the promissory note and the deed of trust that allows the lender to call the balance due and payable in full upon default is known as
  - A. the due-on-sale clause.
  - B. the satisfaction clause.
  - C. the acceleration clause.
  - D. the alienation clause.
9. The sales price of the property is \$250,000 and the appraised value is \$240,000 at an 80% LTV. What is the loan amount of the property?
  - A. \$192,000
  - B. \$200,000
  - C. \$240,000
  - D. \$250,000
10. Charging an interest rate that exceeds the legal maximum ceiling is known as
  - A. defeasance.
  - B. usury.
  - C. subordination.
  - D. a violation of Regulation Z.
11. A loan amortized over 30 years but due and payable in 10 years is what type of loan?
  - A. ARM
  - B. Package
  - C. Blanket
  - D. Balloon
12. The document that is recorded to give notice that a deed of trust has been paid in full is
  - A. the defeasance.
  - B. the subordination contract.
  - C. the note.
  - D. the reconveyance deed.

13. In a foreclosure, if there are insufficient proceeds, state law may permit the lender to file
  - A. a default judgment.
  - B. a deficiency judgment.
  - C. a declaration.
  - D. a right to cure.
14. A mortgage with a rate that is tied to an economic index and may have interest rate or payment caps is
  - A. a renegotiable-rate mortgage.
  - B. a partially amortized mortgage.
  - C. an adjustable-rate mortgage.
  - D. a variable payment mortgage.
15. All of the following are true of a promissory note EXCEPT
  - A. it is recorded.
  - B. it is evidence of the debt but not security.
  - C. a recorded mortgage or deed of trust is needed to secure the note.
  - D. it has numerous clauses that are the same as the mortgage or deed of trust.
16. The document that creates security for a promissory note could be
  - A. a deed of trust.
  - B. a contract for deed.
  - C. a warranty deed.
  - D. a quitclaim deed.
17. A lender charges four discount points on a \$150,000 loan. The points will
  - A. pay the lender's commission on the loan.
  - B. reduce the LTV and down payment needed.
  - C. decrease the loan amount by 4%.
  - D. increase the lender's yield on the loan.
18. Which type of loan requires interest-only payments until maturity of the principal?
  - A. Blanket loan
  - B. Amortized loan
  - C. Term loan
  - D. Partially amortized loan
19. Which of the following is TRUE of a promissory note?
  - A. It is the same as a deed of trust.
  - B. It is a promise to pay.
  - C. It is security for the deed of trust.
  - D. It is attached to a deed.
20. The fee that is charged by lenders as part of their processing and is similar to a commission is called
  - A. a discount point.
  - B. PMI.
  - C. subordination.
  - D. loan origination.
21. The BEST way to prove payment in full of a loan is
  - A. copies of canceled checks.
  - B. a deed of trust.
  - C. a notice of satisfaction.
  - D. a lender certificate of payment.
22. Interest charged on mortgage loans is typically
  - A. compound.
  - B. floating.
  - C. simple.
  - D. discounted.
23. The acceleration clause in the note and deed of trust
  - A. is used to stop assumption of the loan.
  - B. allows the lender to demand full payment and changes the terms of the loan.
  - C. can be used if the borrower has not maintained the property and therefore is in default.
  - D. automatically accelerates the loan payments if the borrower's payment is a few days late.
24. The loan-to-value ratio (LTV)—the mortgage amount divided by the sales price or appraised value of the property—does NOT determine the
  - A. cost of each discount point.
  - B. amount of the loan origination fee.
  - C. amount of interest for each payment.
  - D. amount of the down payment.

# UNIT 12 BROKER-LEVEL QUESTIONS

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1. A loan that has a 3.5% interest rate for the first three years and then adjusts according to an economic index should NOT be considered by a borrower who
  - A. can put down a high down payment.
  - B. will live in the property less than five years.
  - C. has no expectation of an increase in income.
  - D. expects to receive regular wage increases.
2. A property is under contract for \$200,000 and has appraised for \$210,000. The buyer has requested that the seller pay three points on the 90% LTV loan. What will be the points cost to the seller?
  - A. \$5,400
  - B. \$5,670
  - C. \$6,000
  - D. \$6,300
3. The seller and the buyer have agreed to a purchase price of \$765,000, with the seller acting as the lender. The buyer takes possession of the property but does not have legal title. This is MOST likely an example of
  - A. an installment contract.
  - B. a lease.
  - C. a purchase money loan.
  - D. an option.
4. All of the following clauses in a loan agreement enable the lender to demand the entire remaining debt be paid immediately EXCEPT
  - A. a defeasance clause.
  - B. a due-on-sale clause.
  - C. an acceleration clause.
  - D. an alienation clause.

# UNIT 12 QUIZ ANSWERS

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1. **C** The answer is lender, mortgagee. The lender is the mortgagee; the borrower is the mortgagor.
2. **D** The answer is a mortgage. The document with which real property is pledged as security or collateral for a debt is the mortgage.
3. **B** The answer is the equitable redemption. The period before the foreclosure sale is known as the equitable redemption period.
4. **D** The answer is the original loan amount. Principal is the total or original amount of the loan. Payments are first applied to interest and then to principal.
5. **A** The answer is more than one property is pledged as security for the loan. A blanket mortgage covers two or more parcels of real estate.
6. **A** The answer is the difference between the current market value and the amount owed. Today's value minus today's debt equals today's equity.
7. **C** The answer is borrowers are more likely to default. The disadvantage to high leverage is that the borrower may default on the loan, especially if market values start to drop.
8. **C** The answer is the acceleration clause. The acceleration clause allows the lender to "call the note" upon default.
9. **A** The answer is \$192,000. The LTV is based on the purchase price or the appraised value, whichever is lower. The appraised value was lower, so it will be used to calculate the loan amount, which will be 80% of \$240,000.  $\$240,000 \times 0.80 = \$192,000$ .
10. **B** The answer is usury. Usury rates are set by state law. A loan in which the rate exceeds the legal maximum ceiling is said to be a usurious loan.
11. **D** The answer is balloon. The loan payments are amortized over 30 years, but only 10 years of payments will be made due to the 10-year term. The loan will have a large balloon payment.
12. **D** The answer is the reconveyance deed. The document is called a reconveyance deed of trust, which will release the lien that was created by the original deed of trust and transfer legal title from the trustee back to the borrower.
13. **B** The answer is a deficiency judgment. If the sale proceeds are insufficient to satisfy the debt, the lender may be able to claim a deficiency judgment against the borrower.
14. **C** The answer is an adjustable-rate mortgage. The interest rate on an ARM is subject to change based on increases or decreases in a specific economic index.
15. **A** The answer is it is recorded. The promissory note is not recorded. The mortgage or deed of trust is recorded and creates the lien against the property.
16. **A** The answer is a deed of trust. A deed of trust is a security instrument that creates a lien when recorded.
17. **D** The answer is increase the lender's yield on the loan. Discount points increase the lender's yield on the loan.
18. **C** The answer is term loan. A term loan or straight loan requires interest-only payments until maturity, at which time the entire principal balance must be paid in full.
19. **B** The answer is it is a promise to pay. The note establishes a promise to repay a debt.
20. **D** The answer is loan origination. The loan origination fee is similar to the mortgage loan originator's commission.

21. **C** The answer is a notice of satisfaction. To prove payment in full, a mortgagor would need a satisfaction notice. A deed of trust requires a reconveyance deed. Both documents should be recorded by the borrower.
22. **C** The answer is simple. Simple interest is charged on most mortgage loans—not compound, floating, or discount interest.
23. **C** The answer is can be used if the borrower has not maintained the property and therefore is in default. The acceleration clause may be used any time the borrower is in default, such as not maintaining the property and committing waste. The acceleration clause does not allow the lender to change the terms of the loan or arbitrarily call the note due.
24. **C** The answer is amount of interest for each payment. The LTV is used to determine the loan amount, which in turn determines the cost of each discount point, the loan origination fee, and the amount of the down payment, but not the interest rate.

### Broker-Level Questions

1. **C** The answer is has no expectation of an increase in income. The loan described is an ARM, and because the adjustment can increase the payment, it is not a good choice for those with a set income.
2. **A** The answer is \$5,400. The loan value is based on the sales price or appraised value, whichever is less. The loan value is \$180,000 (90% of \$200,000) and the points are \$5,400 ( $\$180,000 \times 0.03$ ).
3. **A** The answer is an installment contract. An installment contract or contract for deed allows the buyer to take possession but not obtain legal title until the last payment is made. In a lease, the seller is not the lender. An option is the right to buy, but it does not come with the right of possession.
4. **A** The answer is a defeasance clause. The defeasance clause states that upon repayment of the loan, the lender must provide a satisfaction of lien notice that the borrower records, removing the recorded lien from the property.

# UNIT 13

## Government Involvement in Real Estate Financing

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain the primary and secondary mortgage marketplaces, the roles of the parties in each, and the impact on the parties of government influence.
- › Describe the difference between conventional, government, and private loan programs available for real estate financing.
- › Describe the various alternative and special-purpose loan programs that can meet a borrower's specific needs.
- › Explain the primary government regulations that govern real estate lending and provide consumer protection against unfair lending practices.

### KEY POINTS—UNIT 13

- A conventional loan is a mortgage loan that is not insured or guaranteed by a government agency. Conventional loans may require private mortgage insurance (PMI), depending on the loan-to-value ratio (LTV).
- The Federal Housing Administration (FHA) is part of the Department of Housing and Urban Development (HUD). It provides home mortgage insurance, insuring approved lenders against losses resulting from default and foreclosure on FHA-insured loans.
- The U.S. Department of Veterans Affairs (VA) guarantees repayment of certain residential loans made to eligible veterans. Eligibility for VA loans is based on the length of service in one of the U.S. Armed Forces or National Guard.

- In the primary mortgage market, lenders make loans to borrowers. In the secondary or national market, private investors and government-sponsored agencies buy and sell real estate mortgages. This helps to provide funds to the primary market and to moderate the effects of local economic conditions and real estate cycles by transferring money from areas where there is a surplus of loan funds to areas where there is a shortage. Government-sponsored secondary market agencies include the Federal National Mortgage Association (FNMA), Government National Mortgage Association (GNMA), and Federal Home Loan Mortgage Corporation (FHLMC).
- The Truth in Lending Act (TILA) is a federal law that requires lenders to disclose the complete cost of credit to consumer loan applicants. A requirement of the act is that borrowers must be given a three-day right of rescission on home equity loans.
- The Real Estate Settlement Procedures Act (RESPA) regulates lenders and standardizes real estate settlement practices in residential mortgage transactions. The law requires that certain disclosures be made to loan applicants concerning all closing costs the buyer will incur.
- The Consumer Financial Protection Bureau (CFPB) is charged with enforcing both TILA and RESPA.
- Federal laws designed to eliminate discrimination in lending include the Equal Credit Opportunity Act (ECOA) and the Fair Credit Reporting Act.

## I. INTRODUCTION TO THE REAL ESTATE FINANCING MARKET

### A. Federal Reserve System (the Fed)

1. Acts through its Board of Governors
  - a. Maintains sound credit conditions
  - b. Helps counteract inflationary and \_\_\_\_\_ trends
  - c. Works to create a favorable economic climate
2. Regulates the supply of money and interest rates in the United States

### B. Primary mortgage market

1. Institutional and other lenders to consumers
2. Mortgage bankers provide financing; they are \_\_\_\_\_.
3. \_\_\_\_\_ bring together borrowers and lenders.
4. Mortgage loan originators (MLOs)
  - a. Must be \_\_\_\_\_
  - b. Must \_\_\_\_\_ annually and meet other requirements



**C. Secondary mortgage market**

1. Loans are bought and sold after being funded.
2. Secondary market activities
  - a. Real estate loans are \_\_\_\_\_ in the primary market.
  - b. The mortgages are sold in the \_\_\_\_\_, providing money to the primary market to originate more loans.
  - c. Mortgage-backed securities are sold to investors to finance the secondary market.
  - d. Borrowers may be directed to send payments to a different address or company if their mortgage is sold on the secondary market, but the loan terms do not change.
3. Federal National Mortgage Association—FNMA or Fannie Mae
  - a. Buys blocks or \_\_\_\_\_ of mortgages
  - b. Requires \_\_\_\_\_ forms
4. Federal Home Loan Mortgage Corporation—FHLMC or Freddie Mac
  - a. Provides secondary market primarily for \_\_\_\_\_ loans
  - b. Uses standardized forms issued with Fannie Mae
5. Federal Agricultural Mortgage Corporation—Farmer Mac
  - a. Shares are privately owned and publicly traded.
  - b. Deals in \_\_\_\_\_ mortgage and rural utilities loans
6. Government National Mortgage Association—GNMA or Ginnie Mae
  - a. Agency within HUD that guarantees payments on mortgage-backed securities used to buy FHA and VA mortgages

**II. LOAN PROGRAMS****A. Conventional loans**

1. Debt repayment rests on the borrower's willingness and ability to repay.
  - a. Loans are not insured or guaranteed.
2. Conventional loans are the most secure because they tend to have the lowest \_\_\_\_\_ ratio.
3. Typically, maximum LTV is 80% to avoid paying for mortgage insurance.

4. Fannie Mae and Freddie Mac establish borrower and collateral qualifications for loans they purchase.
  - a. \_\_\_\_\_ loans fall within a maximum loan limit that can change annually.
  - b. Nonconforming loans are those above the limit for the conforming loans sold on the secondary mortgage market.
    - i. Also called \_\_\_\_\_
    - ii. May be held in the investor's loan portfolio

### **B. Private mortgage insurance**

1. Private mortgage insurance (PMI) protects lenders from loss due to a deficiency after foreclosure.
2. A borrower/mortgagor pays PMI when the LTV is above \_\_\_\_\_.
  - a. PMI does not pay off the full loan.
    - i. PMI covers a portion of the shortfall between the amount obtained through the foreclosure sale and the outstanding mortgage debt.
  - b. The advantage for the borrower is a \_\_\_\_\_.

### **C. FHA-insured loans**

1. The FHA provides mortgage default insurance.
  - a. Insures the lender against loss due to borrower default
  - b. A mortgage insurance premium (MIP) is paid by the borrower.
  - c. May be paid upfront or financed and paid monthly
  - d. Loan funds come from approved lenders who set the interest rates charged.
  - e. The properties must be \_\_\_\_\_.
2. The FHA allows discount points to be paid, as negotiated by the \_\_\_\_\_.
3. A default on an FHA-insured loan results in a \_\_\_\_\_ by HUD.
  - a. Property is sold in "as-is" condition.
  - b. Early bidding is allowed for bidders who intend to be \_\_\_\_\_.

**D. VA-guaranteed loan program (Department of Veterans Affairs)**

1. The VA \_\_\_\_\_ lenders against losses on loans to eligible veterans.
  - a. Eligible veterans: active military, National Guard members, veterans, or retired military reserve members
  - b. No insurance premium
  - c. Has a funding fee that can be financed
  - d. No prepayment penalty or due-on-sale clause
2. The veteran \_\_\_\_\_ the property as a home.
3. Loan-to-value ratio can be up to \_\_\_\_\_.
4. VA requires the following two certificates:
  - a. Certificate of eligibility/entitlement
  - b. Certificate of reasonable value (CRV)
5. The purchase contract must contain a VA financing contingency clause.
6. The lender's approval is required for assumption.
7. Nonveterans may assume a VA-guaranteed loan.

**III. OTHER FINANCING TECHNIQUES****A. Package loan**

1. Includes \_\_\_\_\_ property
2. Popular with developers and purchasers of \_\_\_\_\_

**B. Blanket loan**

1. Covers more than one parcel or lot
2. Usually contains a \_\_\_\_\_

**C. Open-end loan**

1. Secures \_\_\_\_\_ of funds from lender to borrower
2. Allows the borrower to increase the debt to the original amount or the stated maximum

**D. Construction loan**

1. Made to finance \_\_\_\_\_ to real estate
2. Generally have short-term or \_\_\_\_\_ financing
3. Replaced by a permanent loan, also known as an \_\_\_\_\_ or \_\_\_\_\_ loan

**E. Sale-and-Leaseback**

1. The seller frees capital by selling property, then \_\_\_\_\_ it back from the buyer.
2. Usually involves both land and building

**F. Buydown**

1. A way to \_\_\_\_\_ the interest rate on a loan
2. Can be temporary or \_\_\_\_\_
3. Can be paid by the borrower or someone else

**G. Home equity loan**

1. The original mortgage loan \_\_\_\_\_ .
2. A home equity loan is \_\_\_\_\_ .
3. The interest on a home equity loan of up to \_\_\_\_\_ is deductible from federal income tax.
4. Can take the form of a line of credit, referred to as a(n) \_\_\_\_\_

**IV. FINANCING LEGISLATION****A. Truth in Lending Act and Regulation Z**

1. Regulation Z was created by the Federal Reserve Board to enforce the Truth in Lending Act (TILA).
  - a. TILA applies to all consumer lending, not just real estate.
  - b. Regulation Z generally applies when a credit transaction is secured by \_\_\_\_\_.
  - c. Annual percentage rate (APR) = true cost of credit and lender charges
2. The purpose of the Truth in Lending Act is to promote the informed use of consumer credit by requiring advance disclosure of loan terms and costs.
  - a. A creditor is any person who extends consumer credit more than \_\_\_\_\_ or if the transactions involve dwellings as security more than \_\_\_\_\_.
  - b. The credit must be subject to a finance charge or payable in more than \_\_\_\_\_ by written agreement.

## 3. Consumer Financial Protection Bureau (CFPB)

- a. Created by the Dodd-Frank Act
- b. Now responsible for most TILA enforcement

## 4. Right of rescission

- a. TILA requires a \_\_\_\_\_ for refinances of owner-occupied, one- to four-unit properties and home equity loans.
- b. Rescission does not apply to home \_\_\_\_\_.

## 5. Advertising requirements

- a. The asking price and APR are the only finance terms allowed in an advertisement without full disclosure.
- b. The mention of down payment, interest rate, monthly payment, or number of payments \_\_\_\_\_ (the small print).
- c. General statements not related to financing are allowed.

## 6. Remember

- a. Truth in Lending Act = disclosure of \_\_\_\_\_
- b. RESPA = disclosure of \_\_\_\_\_ to close

## 7. Penalties for failure to comply with TILA

- a. The creditor may be liable to a consumer for actual damages and the cost of any legal action plus attorney's fees.
- b. In other actions, a creditor may be liable to a consumer for twice the amount of the finance charge, at a minimum of \_\_\_\_\_ up to a maximum of \_\_\_\_\_ plus court costs, attorney's fees, and actual damages.
- c. A class action could result in making the creditor liable for punitive damages of the lesser of \_\_\_\_\_ or 1% of the creditor's net worth plus attorney's fees and court costs.
- d. In addition to monetary penalties, a willful violation of TILA is a \_\_\_\_\_ punishable by a fine of up to \$5,000, one year's imprisonment, or both.

**B. Equal Credit Opportunity Act (ECOA)**

- 1. The purpose of ECOA is to make consumer credit available with fairness and impartiality.
  - a. Membership in a protected class should have no bearing on qualifying for a loan.

2. Prohibits discrimination in all consumer credit transactions
  - a. Protected categories include race, color, religion, national origin, sex, marital status, dependence on public assistance, and \_\_\_\_\_.
  - b. To fair housing categories, ECOA adds the protected classes of \_\_\_\_\_.
  - c. ECOA does not protect those with an erratic employment history or bad credit.
3. The lender is required to provide a written notice of why a borrower was denied a loan.

### **C. Community Reinvestment Act of 1977 (CRA)**

1. The CRA refers to the responsibility of financial institutions to help meet community needs for \_\_\_\_\_ housing. Financial institutions are expected to
  - a. meet deposit and credit needs;
  - b. participate and invest in \_\_\_\_\_ projects; and
  - c. participate in loan programs for housing, small businesses, and \_\_\_\_\_.
2. A federally regulated financial institution must
  - a. prepare a statement that defines the community and identifies the institution's programs; and
  - b. post a public notice that the institution's community reinvestment activities are subject to \_\_\_\_\_ and those reviews must be made public.

### **D. Real Estate Settlement Procedures Act (RESPA)**

1. RESPA standardizes closing practices for a new first mortgage loan on one- to four-family residential properties financed by federally related loan lenders.
  - a. Includes FHA, VA, and conventional loans
  - b. Ensures buyers and sellers receive information of all settlement costs
  - c. Also requires an estimate of a loan cost at application and disclosure of loan costs at closing
2. Automated \_\_\_\_\_ procedures shorten loan process time.
3. Underwriters must consider the following:
  - a. Collateral, including house value, down payment, and \_\_\_\_\_
  - b. Credit reputation, with \_\_\_\_\_ being just one consideration
  - c. Capacity, which includes \_\_\_\_\_

## UNIT 13 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

100%	ECOA	primary mortgage market
age	FHA	private mortgage insurance
all closing costs	kickback	(PMI)
annual percentage rate (APR)	Loan Estimate (LE)	Regulation Z
certificate of eligibility	occupy	secondary mortgage market
certificate of reasonable value	prepayment	three business days
Closing Disclosure (CD)	price	VA

1. A uniform measure of the cost of credit that includes interest and finance charges is known as the \_\_\_\_\_.
2. The market where loans are originated for consumers is known as the \_\_\_\_\_.
3. An agency of the federal government that guarantees loans made to veterans is the \_\_\_\_\_.
4. A government agency that insures (but does not make) mortgage loans is the \_\_\_\_\_.
5. Refusing to make a mortgage loan because the applicant is 80 years old is a violation of \_\_\_\_\_.
6. Loans are sold to support additional consumer loans in the \_\_\_\_\_.
7. ECOA adds protection from discrimination based on \_\_\_\_\_, which is not protected under fair housing law.
8. The type of mortgage insurance that lenders require on conventional loans exceeding an 80% LTV is called \_\_\_\_\_, which provides lenders additional protection in case of default.
9. VA loans feature a loan-to-value ratio (LTV) of up to \_\_\_\_\_, meaning qualified veterans may purchase a home with little or no down payment.
10. A consumer protection law that requires lenders to disclose the true cost of obtaining credit is \_\_\_\_\_, which implemented the Truth in Lending Act (TILA) requiring disclosure of the annual percentage rate (APR) in advertising.
11. The Real Estate Settlement Procedures Act (RESPA) requires disclosure of \_\_\_\_\_ in all one- to four-unit residential transactions using a federally related loan.
12. According to the Truth in Lending Act, \_\_\_\_\_ and \_\_\_\_\_ are the only financial terms that can be advertised without triggering full disclosure.

## UNIT 13 GLOSSARY REVIEW ANSWERS

1. annual percentage rate (APR)
2. primary mortgage market
3. VA
4. FHA
5. ECOA
6. secondary mortgage market
7. age
8. private mortgage insurance (PMI)
9. 100%
10. Regulation Z
11. all closing costs
12. price, annual percentage rate (APR)



# UNIT 13 QUIZ

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1. FHA insurance is designed to protect
  - A. the mortgagor.
  - B. the lender.
  - C. the seller.
  - D. the broker.
2. A 100% LTV is a feature of many
  - A. FHA-insured loans.
  - B. VA-guaranteed loans.
  - C. conventional loans.
  - D. conventional guaranteed loans.
3. A borrower might choose to pay private mortgage insurance (PMI) to
  - A. have more equity.
  - B. reduce the monthly payment.
  - C. have a lower LTV.
  - D. bring a smaller down payment to closing.
4. Which of the following loans would be subject to a right of rescission?
  - A. Purchase of a new home
  - B. Home equity loan
  - C. Construction loan for a home
  - D. Purchase of a second home
5. The primary function of the secondary mortgage market is to
  - A. grant new loans.
  - B. purchase mortgages from the primary market.
  - C. purchase contracts for deed.
  - D. insure mortgages.
6. Which of the following statements about the annual percentage rate is TRUE?
  - A. It is the disclosure of the face rate as required by Regulation Z.
  - B. It is the interest rate stated on the note.
  - C. It includes the nominal interest rate and finance charges.
  - D. It shows that the true cost of financing is always lower than the note rate.
7. The federal law that adds age as a protected class is
  - A. the FHA.
  - B. the Equal Credit Opportunity Act (ECOA).
  - C. Federal National Mortgage Association (FNMA).
  - D. the Real Estate Settlement Procedures Act (RESPA).
8. Interest rates are MOST likely to be impacted by
  - A. government loan insurance programs like the FHA's.
  - B. government guarantees on loans to veterans.
  - C. depreciation and capital gains laws.
  - D. policies set by the Federal Reserve.
9. Which entity offers VA and FHA loans to borrowers?
  - A. VA- and FHA-approved lenders
  - B. VA or FHA, depending on which loan is chosen
  - C. HUD
  - D. Any local bank or mortgage broker
10. If a qualified borrower is refused a loan because the borrower is retired and receiving public assistance, the lender is in violation of
  - A. HUD.
  - B. RESPA.
  - C. FHA.
  - D. ECOA.
11. The LTV determines the maximum loan amount based on
  - A. the lower of the sales price or appraised value.
  - B. the sales price only.
  - C. the appraised value only.
  - D. the higher of the sales price or appraised value.
12. Purchasers using an FHA-insured loan to buy a home will pay an FHA insurance premium called
  - A. private mortgage insurance (PMI).
  - B. a mortgage insurance premium (MIP).
  - C. conventional mortgage insurance (CMI).
  - D. a conventional premium index (CPI).

13. The purpose of Regulation Z is to
  - A. promote the informed use of consumer credit by requiring disclosures of loan terms and costs.
  - B. provide financing opportunities for underserved communities.
  - C. require lenders to inform consumers of all closing costs.
  - D. prohibit kickbacks to real estate agents for referral of closing services.
14. The Truth in Lending Act and Regulation Z require the disclosure of a lender's effective interest rate, calculated by adding the impact of loan fees and discount points to the nominal or face rate of a loan. The rate is called
  - A. the maximum percentage rate (MPR).
  - B. the nominal percentage rate (NPR).
  - C. the loan-to-value rate (LTV).
  - D. the annual percentage rate (APR).
15. What financing terms can be advertised without triggering all the financing disclosures required by Regulation Z?
  - A. Price and down payment
  - B. Price and APR
  - C. Monthly payments and APR
  - D. Price, interest rate, term, and monthly payments
16. Which would be a violation of the Equal Credit Opportunity Act (ECOA)?
  - A. Using different underwriting standards for families with children
  - B. Refusing to take a loan application from a minor (under the age of 18)
  - C. Charging higher interest and discount points based on credit and employment history
  - D. Refusing to lend to applicants over the age of 72
17. Which of the following are NOT representative of the annual percentage rate (APR)? The APR
  - A. will always be higher than the face rate or nominal interest rate.
  - B. determines the loan-to-value ratio (LTV).
  - C. adds the impact of loan fees, discount points, and interest rate.
  - D. is the effective rate being paid by the borrower.

# UNIT 13 BROKER-LEVEL QUESTIONS

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1. A property sold for \$300,000 and was appraised for \$310,000, and the borrower is getting an 85% LTV conventional loan. All of the following are true about the loan EXCEPT
  - A. the borrower will most likely need to pay PMI to get the loan.
  - B. the LTV will be based on the appraised value.
  - C. the down payment will be \$45,000.
  - D. the lender will require the borrower to occupy the property.

# UNIT 13 QUIZ ANSWERS

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1. **B** The answer is the lender. The lender's unpaid balance is insured by the FHA against losses resulting from the borrower's default.
  2. **B** The answer is VA-guaranteed loans. The VA-guaranteed loan program is one of only a few types that allows a 100% LTV.
  3. **D** The answer is bring a smaller down payment to closing. A borrower would choose to pay PMI to have a higher LTV and bring less down payment to closing.
  4. **B** The answer is home equity loan. Refinances of owner-occupied, one- to four-unit properties and home equity loans require a three-day right of rescission. Rescission does not apply to home purchases or construction loans.
  5. **B** The answer is purchase mortgages from the primary market. The primary purpose of the secondary mortgage market is to purchase mortgages from the primary market, which provides funding to the primary market.
  6. **C** The answer is it includes the nominal interest rate and finance charges. The APR includes the nominal (note or face) rate, plus other finance charges.
  7. **B** The answer is the Equal Credit Opportunity Act (ECOA). The ECOA adds age, marital status, and receipt of public assistance as protected classes, but does not protect minors, familial status, or erratic employment history.
  8. **D** The answer is policies set by the Federal Reserve. Federal Reserve policies have the most impact on interest rates.
  9. **A** The answer is VA- and FHA-approved lenders. FHA and VA loans may be obtained only from approved primary lenders.
  10. **D** The answer is ECOA. ECOA, the Equal Credit Opportunity Act, does not allow discrimination in lending based on age or the receipt of public assistance. If the person receiving assistance qualifies, then the loan must be made.
  11. **A** The answer is the lower of the sales price or appraised value. Lenders determine the maximum loan by applying the LTV to the lower of the sales price or appraisal.
  12. **B** The answer is a mortgage insurance premium (MIP). FHA borrowers pay a MIP that is in addition to monthly loan payments.
  13. **A** The answer is promote the informed use of consumer credit by requiring disclosures of loan terms and costs. Regulation Z applies to all consumer credit offerings and requires disclosure of all fees and terms associated with financing.
  14. **D** The answer is the annual percentage rate (APR). The APR is the effective rate a lender earns when loan fees, discount points, and other loan costs are added to the nominal interest rate.
  15. **B** The answer is price and APR. Under the Truth in Lending Act's Regulation Z, price and APR are the only financing terms that can be advertised without triggering the full disclosure required by law.
  16. **D** The answer is refusing to lend to applicants over the age of 72. The ECOA adds age as a protected category. Minors lack the contractual capacity required to sign lending documents.
  17. **B** The answer is the APR determines the loan-to-value ratio (LTV). The APR is the effective rate the lender earns by charging interest, loan origination fees, discount points, and other loan charges. The APR has no impact on the LTV.
- ### Broker-Level Questions
1. **B** The answer is the LTV will be based on the appraised value. The loan will be based on the sales price, which is lower. For conventional loans above an LTV of 80%, the borrower must occupy the property and will need to pay PMI.

# UNIT 14

## Closing the Real Estate Transaction

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the steps required to achieve conveyance of clear and marketable title, including compliance with all applicable laws.
- › Describe closing procedures and the respective roles of all parties.
- › Explain the Real Estate Settlement Procedures Act (RESPA) and the Mortgage Disclosure Improvement Act (MDIA).
- › Identify all buyer and seller charges and credits contained in a closing statement.
- › Explain the financial entries and mathematical calculations contained in a closing statement.

### KEY POINTS—UNIT 14

- There are two common methods to close real estate transactions: face-to-face closings (also known as roundtable closings) and escrow closings.
- Face-to-face closings are generally held at a title company, a lender location, an attorney's office, or a brokerage, but could be held anywhere. The closing is conducted by a closer or closing agent and is attended by the buyer, the seller, and their respective real estate professionals and attorneys. Representatives from the lender and title insurance companies may also attend.
- Escrow closings are conducted by a neutral third party. Instead of meeting, all required documents are sent by the parties to the escrow agent who completes the transaction per the terms of the purchase contract. The parties to the transaction never meet.
- Laws require that a detailed closing statement be provided to buyers and sellers in real estate transactions. A credit on the closing statement generally means the party is receiving money, while a debit means the party owes money. For example, the selling price will be shown as a credit to the seller and a debit to the buyer (buyer owes, seller receives).

- Prorating is the dividing of expenses between the buyer and seller. Property taxes and utilities are examples of items that are typically prorated. Certain real estate expenses, such as property taxes and utilities, are paid annually, semiannually, quarterly, or monthly. These costs are divided between the seller and the buyer at closing. The buyer will pay their share of any expense the seller paid in advance, and the seller will pay their share of any expense that the buyer will be charged in arrears.

## I. PRECLOSING PROCEDURES

### A. Buyer's concerns

1. The buyer usually reserves the right to make a \_\_\_\_\_, often called a walk-through, of property being purchased.
2. Information about the exact location and size of the property is provided by a \_\_\_\_\_.
  - a. Indicates location of all buildings, driveways, fences, and other improvements
  - b. Also indicates any existing \_\_\_\_\_.
  - c. The cost of the survey is \_\_\_\_\_.
3. The buyer and the buyer's lender will require the seller to provide some form of \_\_\_\_\_ to show the seller's ownership of the property.

### B. Seller's concerns

1. Assurance that the buyer has the necessary \_\_\_\_\_ to complete the purchase
2. Completion of the tasks required by the \_\_\_\_\_

### C. Real estate professional's role at closing

1. Relatively little if the client has an \_\_\_\_\_
2. Usually attends the \_\_\_\_\_

### D. Lender's interest in closing

1. May require a survey, an inspection report, or, for new construction, a \_\_\_\_\_
2. Will require a buyer to provide a \_\_\_\_\_
3. Typically will request the buyer establish a reserve account for \_\_\_\_\_

### E. Internal Revenue Service reporting requirements

1. Form 1099-S is required on sale or exchange of the following:
  - a. Improved or unimproved land, including air space
  - b. An inherently permanent \_\_\_\_\_

- c. Condominium and its appurtenant features and common elements
- d. Shares in a \_\_\_\_\_

## II. CONDUCTING THE CLOSING

- Closing practices vary widely across the country.
- There are two common methods to close real estate transactions.

### A. Face-to-face closing

1. Held in the office of the title company, lender, attorney, or broker
2. Conducted by a representative of the escrow company or other closing agent
3. Attended by the buyer, the seller, and their real estate agents
4. Attended by the seller's and buyer's \_\_\_\_\_
5. Representatives from the lender and title insurance companies may also attend.

### B. Escrow closing

1. Escrow agent
  - a. A disinterested third party authorized to coordinate closing activities
  - b. Completes the transaction according to the terms in the purchase contract
2. The parties to the transaction never meet.
3. The buyer and seller deposit all pertinent documents and other items with the escrow agent before the \_\_\_\_\_.

## III. LEGISLATION RELATED TO CLOSING

### A. Real Estate Settlement Procedures Act (RESPA)

1. Applies to a first-lien residential mortgage loan made to finance the purchase of a \_\_\_\_\_ for either investment or occupancy
2. Also applies to a second or subordinate lien for a home equity loan when a purchase is financed by a \_\_\_\_\_.
3. RESPA does allow an \_\_\_\_\_ between a real estate brokerage and a mortgage company or other settlement service provider.
4. RESPA places a limit on the amount the borrower is required to deposit in an \_\_\_\_\_.

**B. TILA-RESPA Integrated Disclosure Rule (TRID)**

1. The Truth in Lending Statement and Good Faith Estimate have been replaced by the \_\_\_\_\_ form.
2. The HUD-1 Settlement Statement and the final Truth in Lending Statement have been replaced by the \_\_\_\_\_ form.
3. The information booklet \_\_\_\_\_ must be provided by a creditor to a mortgage applicant as part of the loan application process.

**C. Kickbacks and referral fees**

1. RESPA prohibits the payment of kickbacks, or unearned fees, in any real estate settlement service.
2. RESPA prohibits a \_\_\_\_\_ when no services are actually rendered.

**D. Mortgage Disclosure Improvement Act (MDIA)**

1. If APR increases more than 0.125% from the rate stated in the Closing Disclosure, creditor must provide a new disclosure and wait an additional \_\_\_\_\_ before closing the loan.
2. Consumer may accelerate the process in the event of a personal emergency.

**IV. PREPARATION OF CLOSING STATEMENTS****A. How the closing statement works**

1. A \_\_\_\_\_ is a charge that a party owes and which must be paid at closing, if not paid earlier.
2. A \_\_\_\_\_ is an amount entered in a person's favor.
  - a. An amount that has already been paid
  - b. An amount being reimbursed
  - c. An amount the buyer promises to pay in the form of a loan

**V. PRORATIONS****A. General rules for prorating**

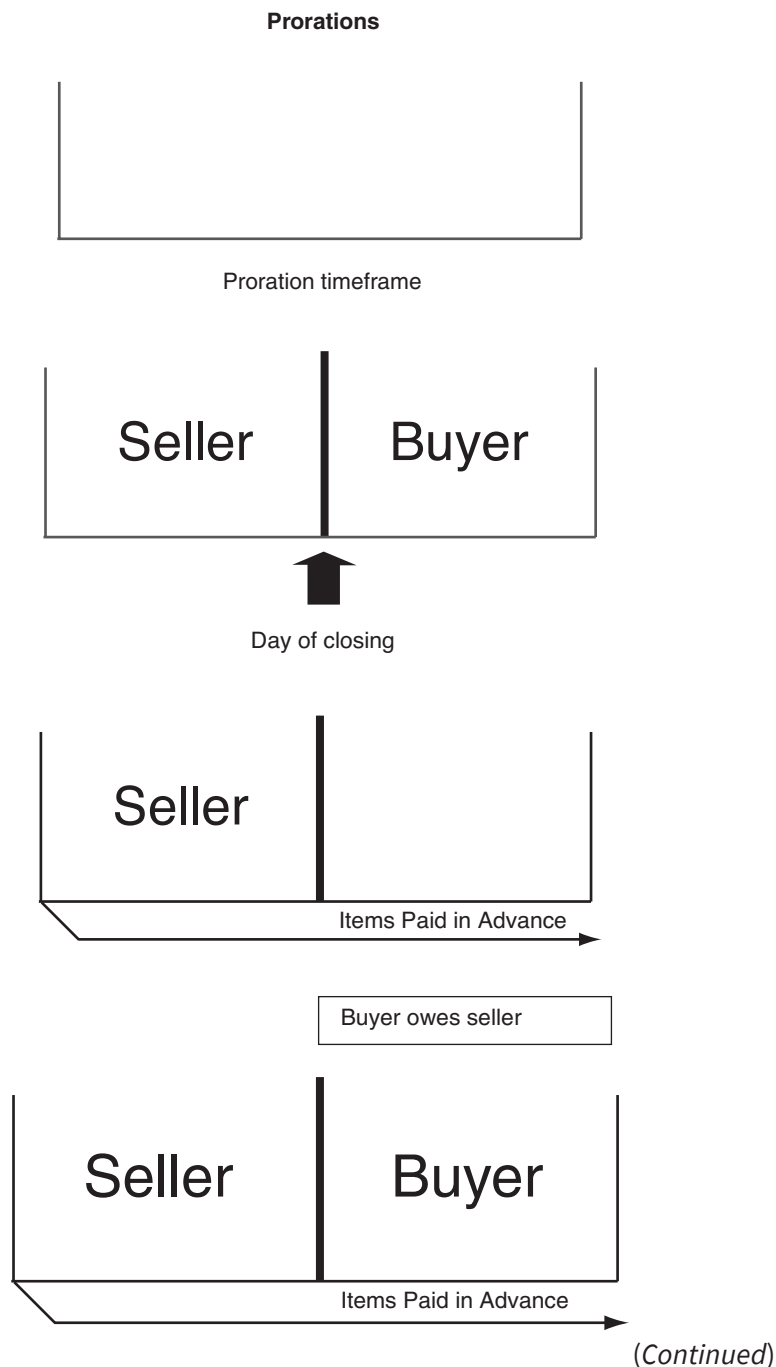
1. Certain costs are prorated (divided between the buyer and the seller) as of the date of closing.
  - a. These costs include things such as property taxes, utilities, HOA dues, and rents (income property).
2. If the seller paid (items paid in advance), calculate the amount owed by the buyer.
3. If the buyer paid (items paid in arrears), calculate the amount the seller owes the buyer.

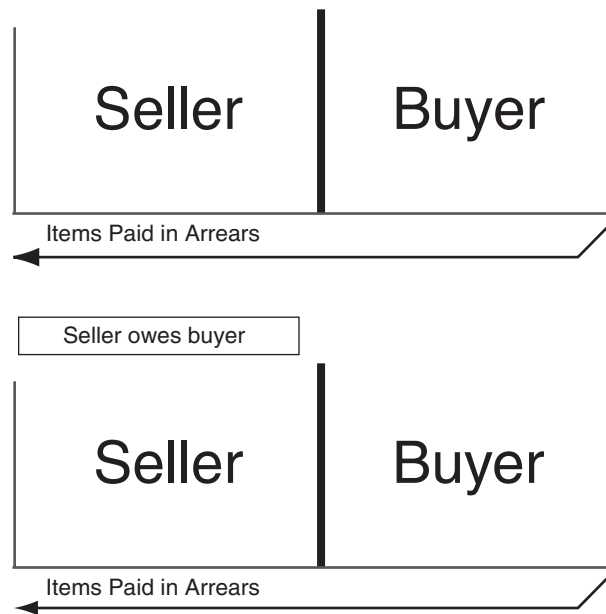
■ Remember: The party that paid the expense will receive a credit at settlement.



4. The prorated amount will always be \_\_\_\_\_.
  - a. The debit (–) to one party will equal the credit (+) to the other.
  - b. Example: The seller owes property taxes of \$860 to the buyer, so debit the seller \$860 and credit the buyer \$860.
5. Rent will be prorated, but security deposits will not.
  - a. The full deposit transfers to the new owner.

**Figure 14.1: Proration Calculations**

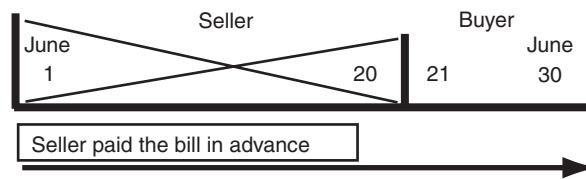


**Figure 14.1: Proration Calculations (continued)****B. The arithmetic of prorating**

1. To calculate prorations:  $(\text{amount paid} \div \text{days in the billing period}) \times \text{number of days owed}$
2. A proration may use a 360-day year, meaning 30-day months, or a 365-day year—the actual number of days in a month. A problem should stipulate which party is responsible for the day of closing.

**C. Practice question**

1. The sale of an investment property closed on June 20, with the seller paying for the day of closing. The \$60 trash bill for the month was paid in advance. How will it be prorated at closing?



- a. The seller paid for the entire month. The buyer owes the portion of the month from June 21 to 30.
- b. To find the days the buyer owes, subtract the total days in the period from the \_\_\_\_\_:  $30 - 20 = 10$  days.
- c. The formula is always the same:
  - i.  $(\text{amount} \div \text{total days}) \times \text{days owed} = \$$
  - ii.  $(\$60 \div 30) \times 10 \text{ days} = \$$
  - iii.  $\$2 \times 10 \text{ days} = \$20$

The buyer owes the seller, so \_\_\_\_\_ the buyer \$20 and \_\_\_\_\_ the seller \$20.

## UNIT 14 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

advance	credit	expenses
arrears	debit	prorated
buyer	equal	seller
Closing Disclosure form	escrow agent	

1. When prorating, an expense paid in advance by the seller will be a(n) \_\_\_\_\_ to the buyer.
2. A prorated expense paid in \_\_\_\_\_ by the buyer will result in a(n) \_\_\_\_\_ to the buyer.
3. A new loan will always be shown as a buyer \_\_\_\_\_ on the closing statement.
4. Certain expense items, such as property taxes and water bills, are often \_\_\_\_\_ between the buyer and the seller as of the day of closing.
5. Each party to the transaction receives a \_\_\_\_\_, which is a detailed accounting of the buyer's and seller's credits and debits, cash required from the buyer, and cash proceeds to the seller.
6. The sales price will be shown on the Closing Disclosure form as a \_\_\_\_\_ to the seller and a \_\_\_\_\_ to the buyer.
7. The Closing Disclosure form will always show \_\_\_\_\_ as debits to a party.
8. Brokerage fees, loan payoff, seller contribution, and a contract for deed will be shown as debits to the \_\_\_\_\_.
9. Earnest money will appear on the closing statement as a \_\_\_\_\_ credit.
10. A disinterested third party authorized to coordinate closing activities is the \_\_\_\_\_, who completes the transaction according to the terms in the purchase contract.
11. Any prorated item will be shown on the closing statement as a credit to one party and an \_\_\_\_\_ debit to the other party.

## UNIT 14 GLOSSARY REVIEW ANSWERS

1. debit
2. arrearage, credit
3. credit
4. prorated
5. Closing Disclosure form
6. credit, debit
7. expenses
8. seller
9. buyer
10. escrow agent
11. equal

# UNIT 14 QUIZ

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1. All of the following would generally be prorated at closing EXCEPT
  - A. rents.
  - B. taxes.
  - C. security deposits.
  - D. water bills.
2. The sales price of the property will be shown on the closing statement as
  - A. debit buyer, credit seller.
  - B. debit buyer, debit seller.
  - C. credit buyer, credit seller.
  - D. debit seller, credit buyer.
3. Monthly owners association dues of \$900 were paid in advance on the first of the month. For a closing on October 20, using a 360-day year and the seller owning the day of closing, the dues would be prorated as
  - A. debit buyer \$300, credit seller \$300.
  - B. debit seller \$300, credit buyer \$300.
  - C. credit buyer \$600, debit seller \$600.
  - D. credit seller \$600, debit buyer \$600.
4. A prorated item that has been paid in arrears will be shown on the closing statement as
  - A. debit buyer, credit seller.
  - B. debit seller, credit buyer.
  - C. debit seller, credit broker.
  - D. debit seller, debit buyer.
5. An item that has been paid in advance will be shown on the closing statement as
  - A. debit buyer, credit seller.
  - B. debit seller, credit buyer.
  - C. debit seller, credit broker.
  - D. debit seller, debit buyer.
6. A disinterested third party is authorized to coordinate closing activities and complete the transaction according to the terms in the purchase contract. The disinterested third party is
  - A. a sales agent.
  - B. an attorney-in-fact.
  - C. a proration agent.
  - D. an escrow agent.
7. A closing is held in an office, conducted by a closer, and attended by the buyer, seller, and possibly other real estate professionals. What type of closing is it?
  - A. Escrow closing
  - B. Face-to-face closing
  - C. Immediate closing
  - D. None of these

# UNIT 14 QUIZ ANSWERS

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1. **C** The answer is security deposits. Security deposits are not prorated. The full amount is transferred from the investment property seller to the buyer.
2. **A** The answer is debit buyer, credit seller. The sales price is a debit from the buyer, who agreed to pay the price, and a credit to the seller, who receives the price.
3. **A** The answer is debit buyer \$300, credit seller \$300. Items paid in advance by the seller will result in a debit to the buyer and an equal credit to the seller, so debit the buyer and credit the seller \$300 for the portion of the month the buyer will own the property ( $\$900 \text{ total dues} \div 30 \text{ total days} \times 10 \text{ days the buyer owns the property} = \$300$  debit buyer, credit seller).
4. **B** The answer is debit seller, credit buyer. Items paid by the buyer in arrears will result in a prorated obligation of the seller. The buyer will be paying the bill sometime in the future, so at closing, the seller will have to give the portion the seller owes to the buyer.
5. **A** The answer is debit buyer, credit seller. Items paid in advance by the seller will be a prorated obligation of the buyer. The seller paid the bill before closing to a date after closing; the buyer will owe the seller for this portion of the month.
6. **D** The answer is an escrow agent. In states that practice escrow closings, the parties to the transaction never meet to attend a closing.
7. **B** The answer is face-to-face closing. Also called a round table closing, a face-to-face closing features the parties to the transaction meeting together to close the transaction.

# UNIT 15

## Real Estate Taxes and Other Liens

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the characteristics of statutory and equitable liens.
- › Describe general taxes and special assessment taxes.
- › Explain real property liens, including judgments and taxes, as well as the protection and limitations they offer the respective parties.

### KEY POINTS—UNIT 15

- Real estate taxes, also called property taxes, are paid to the county where the property is located.
- Payment of property taxes is enforced by a lien. The property tax lien has priority over all other liens, including other government liens. Nonpayment of property taxes can lead to property forfeiture.
- Property taxes are calculated using the property's assessed value, not the actual market value. The assessed value is determined by the county assessor. The property owner may appeal the assessed value to a board of appeals.
- Special assessments are charges against specific properties that benefit from a public improvement, such as installation or replacement of street lighting, sidewalks, pavement, curb and gutter, and so on.
- The special assessment lien is second only to the property tax lien.
- Property tax and special assessment liens are examples of involuntary liens or statutory liens. These liens are created by law, not voluntarily by signing a contract such as a mortgage.
- Mechanics' liens or construction liens are involuntary (statutory) liens for labor, skill, materials, and equipment used for the improvement of real estate. They are available to engineers, architects, surveyors, general contractors, subcontractors, and material or equipment suppliers.
- Voluntary liens are created with the property owner's consent, such as a mortgage pledging property as security for a debt.

- Specific liens attach to a property, not a person. Examples of specific liens include property taxes, special assessments, mortgages, and mechanics' liens.
- General liens, such as a judgment lien for debts owed, are issued by a civil court and attach to a person (or an entity) and everything owned by the person.

## I. LIENS

### A. Purpose of lien

1. A lien is a charge or claim against a person's property made to enforce \_\_\_\_\_.
2. All liens are \_\_\_\_\_, but not all encumbrances are liens.
3. If a lien is not paid on time, the lienholder can \_\_\_\_\_ on the lien.

### B. Lien classifications

1. A lien can be voluntary or involuntary.
  - a. A lien is \_\_\_\_\_ if it is created intentionally by the property owner.
  - b. A lien is involuntary if it is created \_\_\_\_\_.
    - i. A statutory lien is created by statute.
    - ii. An equitable lien arises out of common law.
2. Release of liens
  - a. A lien \_\_\_\_\_ releases an unrecorded lien (construction—mechanic's lien).
  - b. Recording a \_\_\_\_\_ releases a recorded lien (mortgage lien).

### C. Lien types

1. Specific liens—attach to specific real or personal property
  - a. Government liens for property taxes or special assessments (involuntary)
    - i. A property tax lien has \_\_\_\_\_ over all other liens.
    - ii. A special assessment lien has second priority.
    - iii. Other government liens have third priority.
  - b. Mechanic's or construction lien (involuntary)—lien for labor, skill, materials, or equipment provided for the improvement of real estate
    - i. Statutory lien to secure payment to engineers, architects, surveyors, general contractors, subcontractors, and material or equipment suppliers
    - ii. The \_\_\_\_\_ mechanics' liens before transfer of title.



2. Mortgage lien or deed of trust (voluntary)
  - a. Voluntary pledge of land to secure \_\_\_\_\_
3. General lien attaches to \_\_\_\_\_, including personal and real property
  - a. Judgment lien (involuntary)
    - i. Court-ordered claim against an individual and all that the individual owns
    - ii. Examples: unpaid hospital bills, child support, IRS or state liens for income taxes, DEA liens, etc. (involuntary)

#### **D. Priority of liens**

1. Property taxes
2. Special assessments
3. Other government liens
4. Other liens

## **II. REAL PROPERTY TAX LIENS**

### **A. General rules**

1. Real estate taxes are owed to the county where the property is located and payment is enforced by a \_\_\_\_\_ on the property.
2. A property tax lien usually has priority over \_\_\_\_\_.
3. Property taxes are ad valorem taxes, which means that they are based on \_\_\_\_\_.
  - a.  $\text{Assessed value of property} \times \text{tax rate} = \text{property taxes}$
  - b. The county assessor determines assessed value.
  - c. Appeal of an assessment is first made to a \_\_\_\_\_.
4. Properties exempt from taxation include
  - a. government property (federal, state, local);
  - b. property owned by religious and charitable organizations, and used for that purpose;
  - c. hospitals; and
  - d. educational institutions.

**B. Special assessments**

1. \_\_\_\_\_ are charges against specific properties that benefit from a public improvement, such as street lights, sidewalks, paving, curb and gutter.
  - a. Found by reading an \_\_\_\_\_
  - b. Often charged on a front footage (street front) basis
  - c. If not paid, creates a specific lien with the right of foreclosure
  - d. This lien has second priority after unpaid property taxes.

**III. OTHER LIENS ON REAL PROPERTY****A. Mortgage lien**

1. Specific, voluntary lien on real estate given to lender by borrower as \_\_\_\_\_ for a real estate loan
2. The lender will usually require a preferred lien, called a \_\_\_\_\_.
3. Subsequent liens are called \_\_\_\_\_.

**B. Mechanic's lien**

1. A specific, involuntary lien that gives security to persons or companies that \_\_\_\_\_ or furnish materials to improve real property
2. A \_\_\_\_\_ must be filed in the public record of the county.
3. When work is completed and accounts paid, the owner will ask for a \_\_\_\_\_ to clear the property title.

**C. Judgment**

1. A \_\_\_\_\_ is a decree issued by a court.
2. A judgment is a general, involuntary, equitable lien on both real and personal property owned by the debtor.
3. To enforce a judgment, the creditor must obtain a \_\_\_\_\_ from the court.
4. When real property is sold to satisfy a judgment, the debtor should demand a satisfaction of judgment that can be filed with the recorder to clear the record of the lien.
5. Notice of a pending suit is a \_\_\_\_\_.
6. A \_\_\_\_\_ allows a sheriff or other official to take possession of the property until a lawsuit concludes.

**D. Estate and inheritance tax liens**

1. General, statutory, involuntary liens that encumber a deceased person's real and personal property
2. Usually cleared as part of \_\_\_\_\_

**E. Lien for municipal utilities**

1. Specific equitable, involuntary lien
2. Imposed on a property owner who refuses to pay bills for municipal utility services

**F. Bail bond lien**

1. Real estate used to post bail when someone is charged with a crime
2. Specific, voluntary lien against the owner's real estate

**G. Corporation franchise tax lien**

1. General, statutory, involuntary lien on all real and personal property owned by \_\_\_\_\_
2. Generally levied by a state government as a condition of doing business in the state

**H. IRS tax lien**

1. Results from a person's failure to pay any portion of federal taxes
2. A general, statutory, involuntary lien on all real and personal property held by the delinquent taxpayer
3. Does not supersede previously recorded liens
4. Same rules apply to most state income tax liens

## UNIT 15 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

appeals	priority	specific
assessed value	property tax	tax rate
county	recorded	unrecorded
frontage	satisfaction	voluntary
involuntary	second	
lien waiver	special assessment	

- Property taxes are paid to the \_\_\_\_\_ where the property is located.
- The \_\_\_\_\_ lien has \_\_\_\_\_ over all other liens, including other government liens.
- Property taxes are calculated using the property's \_\_\_\_\_, not the actual market value.
- Assessed value  $\times$  \_\_\_\_\_ = property taxes.
- Installation of street lighting, curb and gutter, or repaving may result in a(n) \_\_\_\_\_ levied against the properties that benefit from the public improvement.
- Property owners seeking a lower assessed value should contact the board of \_\_\_\_\_.
- The special assessment lien is \_\_\_\_\_ in priority to only the property tax lien.
- Construction liens may be released before being recorded by receiving a \_\_\_\_\_ from the lienholder in exchange for payment.
- Once recorded, a lien can be released by recording a \_\_\_\_\_ of lien.
- A lien waiver releases a(n) \_\_\_\_\_ lien, while a satisfaction releases a(n) \_\_\_\_\_ lien.
- A(n) \_\_\_\_\_ lien attaches to a specific piece of property, not the owner of the property.
- Mechanics' liens and property tax liens are \_\_\_\_\_ liens, whereas a mortgage lien is a(n) \_\_\_\_\_ lien.

## UNIT 15 GLOSSARY REVIEW ANSWERS

1. county
2. property tax, priority
3. assessed value
4. tax rate
5. special assessment
6. appeals
7. second
8. lien waiver
9. satisfaction
10. unrecorded, recorded
11. specific
12. involuntary, voluntary

# UNIT 15 QUIZ

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1. Real property taxes are computed based on the property's
  - A. subjective value.
  - B. market value.
  - C. assessed value.
  - D. income value.
2. Failure to pay property taxes may result in
  - A. a specific lien.
  - B. an involuntary lien.
  - C. forfeiture of the property.
  - D. all of these.
3. Arrange the following liens in correct order of priority, with the highest priority first: mortgage lien, property tax lien, special assessment lien.
  - A. Property tax lien, special assessment lien, mortgage lien
  - B. Mortgage lien, special assessment lien, property tax lien
  - C. Special assessment lien, property tax lien, mortgage lien
  - D. Whichever lien was recorded first has the highest priority.
4. A property has a \$200,000 first mortgage, a \$10,000 second mortgage, and property taxes of \$2,000 that are not paid. A special assessment of \$1,500 for sidewalk repairs is also past due. Which is the correct priority order of these liens?
  - A. First mortgage, property taxes, second mortgage, special assessment
  - B. Property taxes, first mortgage, second mortgage, special assessment
  - C. Property taxes, special assessment, first mortgage, second mortgage
  - D. First mortgage, property taxes, special assessment, second mortgage
5. A property is valued at \$125,000. The county assessment rate is 80%, and the annual tax rate is 1%. How much are the annual property taxes?
  - A. \$800
  - B. \$1,000
  - C. \$1,100
  - D. \$1,250
6. A 50 mill rate means the property taxes will be
  - A. \$50 per \$1,000 of assessed value.
  - B. 0.050 times assessed value.
  - C. 5% of assessed value.
  - D. all of these.

# UNIT 15 QUIZ ANSWERS

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1. **C** The answer is assessed value. The assessed value is determined by the county assessor and may be appealed.
2. **D** The answer is all of these. The property tax lien is a foreclosable, involuntary specific lien. Nonpayment may lead to property forfeiture. The lien is attached to the property, and the lien is created by law.
3. **A** The answer is property tax lien, special assessment lien, mortgage lien. The liens for property taxes and special assessments are always prioritized first and second, respectively. The priority of other liens is determined by the date of recording.
4. **C** The answer is property taxes, special assessment, first mortgage, second mortgage. Government liens for property taxes and special assessments are always prioritized first and second, respectively. The priority of other liens is determined by the date of recording.
5. **B** The answer is \$1,000.  
 $\$125,000 \times 0.80 \text{ assessment rate} = \$100,000 \text{ assessed value}$   
 $\$100,000 \times 0.01 \text{ tax rate} = \$1,000 \text{ annual taxes}$
6. **D** The answer is all of these. All of these values are equal to the other.  
 $50 \text{ mill} = \$50 \text{ per thousand of assessed value}$   
 $50 \text{ mill} \div 1,000 = 0.050 \times \text{assessed value}$   
 $0.050 = 5\% \times \text{assessed value}$





# UNIT 16

## Real Estate Appraisal

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain appraisal concepts and the process employed by the appraiser.
- › Differentiate between value and price.
- › Describe the three approaches to value.

### KEY POINTS—UNIT 16

- An appraisal is an opinion of value. For appraisal purposes, value is generally measured in terms of money.
- Appraisers must be licensed by the state. A broker or sales associate may complete a competitive market analysis (CMA) of current and recent property sales and listings, but should make it clear to the client that the CMA is not an appraisal.
- An appraisal is required for all federally related loans—conventional, FHA, or VA loans from any federally regulated lender.
- The four essential elements of value for real property are demand, utility, scarcity, and transferability (use the memory aid “DUST”). If any of these items is weak or missing, the property may have less or even no value.
- The principles of value include the principle of highest and best use, the principle of anticipation, the principle of supply and demand, the principle of substitution, the principle of conformity, and the principle of contribution.
- Steps in the appraisal process include defining the problem; determining the scope of work; gathering and verifying general and specific data, as well as data for each of the appraisal approaches used; applying one or more of the three approaches to value (sales comparison, cost, and income approaches); and weighing each approach (reconciliation) to arrive at a final opinion of value.

- In the sales comparison approach (the method most often used for appraising residential property), the prices of sold properties comparable to the subject property are adjusted in relation to the subject to estimate the market value of the subject property.
- In the cost approach, the appraiser estimates the cost of replacing or reproducing the property improvements, deducts estimated depreciation, and adds the estimated value of the land. Depreciation is a loss in value due to any cause, including physical deterioration, functional obsolescence, and external obsolescence.
- In the income approach, the net operating income generated by the subject property is capitalized using a market-derived rate of return to estimate present value. Real estate sellers and investors make decisions based on the capitalization rate or rate of return of properties.
- Reconciliation is the process in which the appraiser weighs the results of the three methods of valuation to develop a final opinion of value.

## I. APPRAISING

### A. Definition of an appraisal

1. An appraisal is \_\_\_\_\_ of market value based on supportable evidence and approved methods.
  - a. Appraisals are regulated at the state and federal level.
    - i. If required for a transaction, an appraisal must be performed by a licensed or certified appraiser.
    - ii. More accurate than a CMA or broker's price opinion (BPO)
  - b. The *Uniform Standards of Professional Appraisal Practice (USPAP)* set the requirements for appraisals. They are published and periodically reviewed by the Appraisal Standards Board (ASB) of the \_\_\_\_\_.
  - c. The Appraiser Qualifications Board of the Appraisal Foundation sets the minimum state \_\_\_\_\_ criteria for appraisers, including minimum levels of education and experience.

### B. Comparative market analysis

1. Not an appraisal, but a review of the market performed by a real estate professional rather than an appraiser
2. Based on
  - a. recently \_\_\_\_\_ properties;
  - b. properties \_\_\_\_\_ on the market; and
  - c. properties that did not sell.

**C. Broker's price opinion (BPO)**

1. The licensee researches and evaluates comparable properties that have recently sold, are currently on the market, or did not sell.
  - a. It is similar to a CMA, as well as the sales comparison approach used in an appraisal.
  - b. A BPO assists a seller and a buyer in determining value.
2. A broker may charge a fee for the CMA or BPO but should make it clear that it is \_\_\_\_\_.

**D. The appraisal process**

1. Most appraisals seek to estimate market value on behalf of a lender but could also be used by sellers estimating the market value of their property.
  - a. An appraisal is required for \_\_\_\_\_ from federally regulated lenders that are above the designated financial threshold.
  - b. An appraisal is \_\_\_\_\_ for seller financing, though it may be a negotiated part of the transaction.
  - c. An appraisal verifies that the loan amount meets the loan-to-value ratio (LTV) required by the lender.
2. Appraisals are also used for insurance purposes, divorce and probate actions, condemnation proceedings, and when a borrower wants to stop paying \_\_\_\_\_ (80% LTV is reached).
3. An accurate appraisal relies on understanding the nature of the problem and the collection and analysis of the necessary \_\_\_\_\_. The steps in the appraisal process include the following:
  - a. Define the \_\_\_\_\_.
  - b. Determine the \_\_\_\_\_.
  - c. Gather, record, verify, and \_\_\_\_\_ the necessary data.
  - d. Form an \_\_\_\_\_ by each of the three approaches.
  - e. \_\_\_\_\_ values to form a \_\_\_\_\_ opinion of value.
  - f. Report the final opinion of value.
4. Fannie Mae and Freddie Mac rely on the use of the \_\_\_\_\_ (URAR) to handle the large numbers of appraisals that are part of the transactions in which they take part.

## II. VALUE

### A. Essential characteristics of value (DUST)

1. \_\_\_\_\_
  - a. Need or \_\_\_\_\_
  - b. Affordability
2. \_\_\_\_\_ is the property's usefulness for its intended purpose.
3. \_\_\_\_\_
  - a. There is a finite supply of land.
  - b. Land in specific areas usually is very limited.
4. \_\_\_\_\_ refers to the relative ease with which ownership rights can be passed from one person to another.

### B. Market value

■ An estimate of what the market will pay

1. The most \_\_\_\_\_ that a property should bring when
  - a. a willing seller would sell and a willing buyer would buy;
  - b. the property is exposed on the open market for a reasonable time;
  - c. both parties are familiar with the property's uses, defects, and advantages; and
  - d. neither party is under abnormal pressure to sell or buy.
2. \_\_\_\_\_ or what someone actually paid
3. Historic and verifiable fact

### C. Basic principles of value

1. Anticipation
  - a. Real estate values are driven by the anticipation of future benefits.
  - b. The income approach is based on the principle of anticipation.
2. Change refers to the fact that no physical or economic condition \_\_\_\_\_.
3. Competition is created by the interaction of supply and demand when a successful business attracts \_\_\_\_\_.
4. Conformity indicates that values tend to be most stable when properties are similar in style and size.

5. Contribution
  - a. Value is determined by what the market will pay, not by the price of an improvement or the cost of installation.
  - b. Generally, more value is added by repairing than improving.
6. Highest and best use
  - a. The use that produces the \_\_\_\_\_ over time, provided the use is
    - i. physically possible;
    - ii. legally permitted; and
    - iii. economically or financially feasible.
  - b. Can change over time
  - c. Would not be included in a \_\_\_\_\_
7. Increasing and diminishing returns
  - a. The addition of improvements to land and structures tends to \_\_\_\_\_ a property's market value, but only up to a certain point. As long as property value increases, the law of \_\_\_\_\_ applies.
  - b. There is a point at which buyers or renters in the market cannot be expected to pay \_\_\_\_\_ for a property. At that point, the law of \_\_\_\_\_ applies.
8. Plottage is the principle that applies when the consolidation of adjacent lots into a single, larger one produces a greater total land value than the sum of the two sites \_\_\_\_\_.
  - a. The process of merging two separately owned lots under one owner is known as \_\_\_\_\_.
  - b. \_\_\_\_\_ is the increase in value or utility of the combined properties.
9. Regression and progression occur when a property's value decreases or increases based on the properties around it.
  - a. A better-quality property is adversely affected by the presence of a lesser-quality property according to the principle of \_\_\_\_\_.
  - b. The value of a modest home would be higher if it were located among larger, more expensive properties according to the principle of \_\_\_\_\_.
10. Substitution is the most important principle in appraisal.
  - a. Substitution is the basis of the sales comparison approach and used in \_\_\_\_\_.
  - b. In real estate (as for any commodity), the product with the lowest price at the highest value will sell first.
    - i. A buyer will pay no more for a property than the cost of acquiring an equally desirable substitute.
    - ii. To be accurate, all approaches to value must consider what the market will pay.

11. Supply and demand are reflected in the real estate market just as they are in the market for any other product. Prices move opposite of supply and with demand.
  - a. When the supply of similar properties increases, their value \_\_\_\_\_.
  - b. When the demand for similar properties increases, their value \_\_\_\_\_.

### III. THE THREE APPROACHES TO VALUE

#### A. Sales comparison/market data approach

1. Key points
  - a. The most important method for \_\_\_\_\_ and vacant land
  - b. The estimate of value is based on adjusted sales prices of similar properties that recently sold.
2. Subject property
  - a. Property being appraised
  - b. Compared to recently sold \_\_\_\_\_
3. Comparable sales (comps)
  - a. Similar properties that have recently sold
  - b. Adjustments always made to the sales price of a comparable
  - c. Comparables with fewer adjustments generally provide a stronger indication of value.
4. Primary elements of comparison and adjustment
  - a. Property rights
  - b. Financing concessions
  - c. Market conditions
  - d. Conditions of sale
  - e. Market conditions since the date of sale
  - f. Location or area preference
  - g. Physical features and amenities

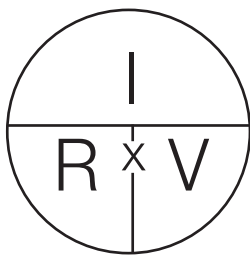
**B. Cost approach**

1. Key points
  - a. The most important method for unique or \_\_\_\_\_, such as churches and schools
  - b. The cost approach is typically used when there are few or no comparable sales.
2. Formula:  $\text{cost to build new} - \text{accrued depreciation} + \text{land value} = \text{estimated value}$
3. Steps to cost approach
  - a. Estimate the value of land as though vacant and at \_\_\_\_\_
  - b. Estimate current cost of constructing buildings and improvements
    - i. The cost to build an exact replica of the subject is its \_\_\_\_\_.
    - ii. The cost to build improvements with the same functional utility is the property's \_\_\_\_\_.
  - c. Estimate the property's accrued depreciation from any of these causes:
    - i. Physical \_\_\_\_\_
    - ii. Functional \_\_\_\_\_
    - iii. External \_\_\_\_\_
  - d. Deduct accrued depreciation from construction cost
  - e. Add estimated land value to depreciated cost of structures and other improvements to derive \_\_\_\_\_ property value

**C. Income approach**

1. Investment properties
  - a. Real estate investors buy for the income the property produces.
  - b. Investors determine what they will pay based on a rate of return or \_\_\_\_\_.
  - c. The capitalization rate (or cap rate) for a property type in a given area can be determined by comparing the net income and selling price of properties sold recently.
  - d. Appraisers use this market-derived capitalization rate to estimate the value of the subject property.

2. Estimate the property's \_\_\_\_\_.
  - a. Current rental income may not reflect current \_\_\_\_\_.
  - b. Potential income also includes from parking, vending machines, and so on.
  - c. Deduct an allowance for vacancy and rent loss to arrive at \_\_\_\_\_
3. Deduct annual operating expenses from effective gross income to arrive at the property's annual \_\_\_\_\_ (NOI)
4. Develop a capitalization rate
  - a. Capitalization math



Income = rate  $\times$  value

I = net operating income (NOI)

R = capitalization rate (investor rate of return, also affected by market forces)

V = value (what can be paid for a property to get the expected return)

Three relationships:

$$I = R \times V$$

$$R = I \div V$$

$$V = I \div R$$

- b. Example 1: A property's annual net income is \$10,000. The appraiser has determined the appropriate cap rate is 10%. What is the estimated market value of the subject property?

$$I = \$10,000$$

$$R = 10\%$$

$$V = I \div R$$

$$\$10,000 \div 0.10 (10\%) = \underline{\hspace{2cm}}$$

The investor can pay \$100,000 for a property earning \$10,000 net and realize the desired yield of 10%.

- c. Example 2: An investor offers \$400,000 for a property earning a 6% rate of return. How much is the net operating income?

$$V = \$400,000$$

$$R = 6\% (0.06)$$

$$I = \$400,000 \times 0.06 = \underline{\hspace{2cm}}$$

- d. Example 3: The net operating income for a property is \$18,000. The property is valued at \$300,000. What is the capitalization rate?

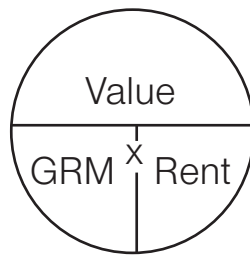
$$I = \$18,000 \div \$300,000 = \underline{\hspace{2cm}}$$

5. Gross rent multiplier (GRM) or gross income multiplier

- a. A simplified alternative to capitalization
  - b. Takes into account gross rent (income) but not vacancies, bad debts, or expenses



- c. Gross rent multiplier is used primarily for single-family rental homes.
- i. Example: Compare the selling price to the gross rent generated by each of the properties
- Comp. 1:  $\$100,000 \text{ price} \div \$10,000 \text{ annual gross rent} = 10 \text{ annual GRM}$
  - Comp. 2:  $\$120,000 \text{ price} \div \$12,000 \text{ annual gross rent} = 10 \text{ annual GRM}$
  - Comp. 3:  $\$115,000 \text{ price} \div \$11,500 \text{ annual gross rent} = 10 \text{ annual GRM}$
  - Comp. 4:  $\$105,000 \text{ price} \div \$10,500 \text{ annual gross rent} = 10 \text{ annual GRM}$
- a. These calculations indicate that properties are selling at 10 times their annual gross rent.
- b. Use this information (annual GRM) to estimate value
- i. The subject property produces \$11,000 annual gross income. What is the value?
  - ii.  $\$11,000 \times 10 \text{ GRM} = \$110,000$
- c. The same approach can be used to determine the monthly gross rent multiplier.



Value = annual or monthly gross rent multiplier multiplied by annual or monthly rent

Three relationships:

Value = GRM  $\times$  rent

Rent = value  $\div$  GRM

GRM = value  $\div$  rent

- i. To solve GRM problems, rent must match the given multiplier.
- If given an annual multiplier and monthly rent, convert monthly rent to annual rent ( $\times 12$ )
  - If given a monthly multiplier and annual rent, convert annual rent to monthly rent ( $\div 12$ )
- d. Formulas (match the multiplier!)
- i. Annual gross rent multiplier  $\times$  annual gross rent = value  
or  
monthly gross rent multiplier  $\times$  monthly gross rent = value
- ii. Example: The monthly gross rent multiplier in the area is 120. If the annual rent is \$12,000, what is the value?
- Match the multiplier:  $\$12,000 \text{ annual gross rent} \div 12 \text{ months} = \$1,000 \text{ monthly gross rent}$   
 $\text{monthly gross rent multiplier} \times \text{monthly gross rent} = \text{value}$   
 $= 120 \times (12,000 \div 12)$   
 $= 120 \times 1,000$   
 $= \$120,000$

## IV. RECONCILIATION

### A. Key points

1. The appraiser reconciles (correlates) the three approaches to value (sales comparison, cost, and income) to arrive at a final estimate of value.
2. Each approach is weighed and used to form an opinion of a subject's market value.  
\_\_\_\_\_.
3. The appraiser considers all three approaches but gives the most weight to the approach that is the most appropriate for the property type.
  - a. For a single-family property, the appraiser would give the most weight to the sales comparison approach.
  - b. For a unique property like a school, the appraiser would give the most weight to the cost approach.
  - c. For an income-producing property like an office building or a shopping center, the appraiser would give the most weight to the income approach.

## UNIT 16 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

capitalization	functional obsolescence	reconciliation
cost approach	income approach	replacement cost
depreciation	market data approach	reproduction cost
economic obsolescence	net operating income	sales comparison approach
effective age	opinion	substitution
external obsolescence	physical deterioration	value

1. The process of converting a future income stream into an expression of present value is income \_\_\_\_\_.
2. The cost of replacing an improvement with another of similar quality but not an exact replica is \_\_\_\_\_.
3. Loss in value due to causes external to the property is \_\_\_\_\_.
4. A method of valuing a property by comparing the subject property to similar properties that have recently sold is the \_\_\_\_\_.
5. Demand, utility, scarcity, and transferability are essential elements of \_\_\_\_\_.
6. An appraisal is an \_\_\_\_\_ of value.
7. To obtain a property's market value using the capitalization approach, an appraiser would divide the \_\_\_\_\_ by the capitalization rate.
8. All the approaches to value use the principle of \_\_\_\_\_.
9. An appraiser calculates accrued depreciation in the \_\_\_\_\_.
10. When an appraiser determines the accrued depreciation, outdated electrical fixtures would be considered \_\_\_\_\_.
11. An appraiser estimating operating expenses is using the \_\_\_\_\_.
12. The market data approach is also known as the \_\_\_\_\_.
13. The step in which the appraiser weighs all approaches to form a final opinion of value is \_\_\_\_\_.
14. An appraiser estimating the value of a shopping center would use the \_\_\_\_\_.
15. The best approach to estimate the value of a library would most likely be the \_\_\_\_\_.

## UNIT 16 GLOSSARY REVIEW ANSWERS

1. capitalization
2. replacement cost
3. external obsolescence
4. market data approach
5. value
6. opinion
7. net operating income
8. substitution
9. cost approach
10. functional obsolescence
11. income approach
12. sales comparison approach
13. reconciliation
14. income approach
15. cost approach

# UNIT 16 QUIZ

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1. Which approach should be used to appraise a 12-year-old, single-family home in a residential neighborhood?
  - A. Sales comparison approach
  - B. Cost approach
  - C. Income approach
  - D. Gross rent multiplier method
2. A property that has a net operating income of \$18,000 and a value of \$200,000 would have a rate of return (capitalization rate) of
  - A. 6%.
  - B. 8%.
  - C. 9%.
  - D. 10%.
3. Which appraisal method considers the cost to build a replacement for the improvements?
  - A. Income approach
  - B. Market data approach
  - C. Cost approach
  - D. Comparison approach
4. A five-bedroom home with one bath is an example of
  - A. functional obsolescence.
  - B. physical deterioration.
  - C. external obsolescence.
  - D. gross rent adjustment.
5. All of these are examples of functional obsolescence EXCEPT
  - A. neighborhood decline.
  - B. an impractical floor plan.
  - C. a two-story home with one bathroom located in the basement.
  - D. a 50-amp electrical service in a residential property.
6. Reproduction cost is defined as
  - A. the current cost to rebuild with the same or highly similar materials.
  - B. replacing an improvement with another that has the same utility.
  - C. the cost determined by the capitalization rate and value.
  - D. none of these.
7. An appraiser would MOST likely rely on the cost approach when appraising
  - A. a single-family home.
  - B. a duplex.
  - C. a church.
  - D. a townhouse.
8. Income capitalization is MOST likely to be associated with the appraisal of
  - A. a condominium project.
  - B. a single-family home.
  - C. an apartment building.
  - D. a townhouse.
9. In the market data approach, adjustments to the comparables are made for all of these EXCEPT
  - A. number of baths.
  - B. square footage.
  - C. time of sale.
  - D. capitalization.
10. The purpose of capitalization is to estimate
  - A. present value based on current or expected income.
  - B. future value based on current gross income.
  - C. present value by multiplying net income by a rent multiplier.
  - D. operating expenses based on the highest and best use.
11. Which principle of value underlies all three approaches to value?
  - A. Change
  - B. Substitution
  - C. Regression
  - D. Aggression
12. A building valued at \$195,000 has a gross income of \$27,000 and expenses of 45%. What is its cap rate?
  - A. 6.2%
  - B. 7.6%
  - C. 13.8%
  - D. 45.0%

13. While writing an appraisal report based on the cost approach, an appraiser referred to "replacement cost new." This is the present cost of replacing the subject improvement with another that
  - A. has the same function and utility.
  - B. uses the same or highly similar materials.
  - C. was built on a similar lot.
  - D. was built in the same year as the subject property.
14. A salesperson has done a BPO for a bank. The salesperson must make sure that the bank understands that
  - A. the opinion is not an appraisal.
  - B. because the salesperson cannot be paid for the opinion, the bank is obligated to list the property with the salesperson.
  - C. the opinion is comparable in scope to an appraisal.
  - D. the opinion is equal to an appraisal and the salesperson will be paid the same as an appraiser.
15. A broker performed a competitive market analysis and determined that the comparable homes are in better overall condition than the seller's property. What adjustments should be made?
  - A. The sales prices of the comparables should be adjusted upward.
  - B. The sales price of the subject should be adjusted upward.
  - C. The sales prices of the comparables should be adjusted downward.
  - D. The listing price of the subject should be the assessed value.
16. Which appraisal method depends on an accurate estimate of the value of the accrued depreciation?
  - A. Reproduction approach
  - B. Market data approach
  - C. Cost approach
  - D. Income approach
17. Which of the following is used to determine the gross rent multiplier?
  - A. Income divided by rent received
  - B. Adjustment to comparable sales
  - C. Sales price and rental rates
  - D. Estimated replacement cost minus depreciation
18. All of the following are essential elements of value EXCEPT
  - A. utility.
  - B. scarcity.
  - C. demand.
  - D. profitability.
19. If the demand for a particular housing style increases, the principle of supply and demand indicates that
  - A. the price will likely decrease.
  - B. the supply will immediately increase.
  - C. the price will likely increase.
  - D. affordability will prohibit any change in price.
20. When an appraiser uses more than one method to estimate value, the process used to arrive at the single final estimate is called
  - A. averaging.
  - B. regression.
  - C. reconciliation.
  - D. capitalization.
21. Progression and regression are part of which principle of value?
  - A. Conformity
  - B. Change
  - C. Substitution
  - D. Contribution
22. An appraiser estimating depreciation is using which approach to value?
  - A. Cost approach
  - B. Income approach
  - C. Market data approach
  - D. Capitalization approach
23. An appraiser reviewing comparables is using which approach to value?
  - A. Cost approach
  - B. Income approach
  - C. Sales comparison approach
  - D. Gross rent multiplier method
24. A broker determined that if the seller will spend \$40,000 in upgrades, the value of the property will increase by \$60,000. Which principle of value did the broker use to make this determination?
  - A. Conformity
  - B. Change
  - C. Substitution
  - D. Contribution

25. Market value is
- A. the same as market price.
  - B. the actual closed price.
  - C. the market price minus sales price.
  - D. the most probable price.
26. The monthly GRM is 120. The annual income is \$24,000. What is the value of the property?
- A. \$24,000
  - B. \$240,000
  - C. \$288,000
  - D. \$2,888,000
27. The formula used in the cost approach is
- A. land minus depreciation plus cost to build new.
  - B. cost to build new minus land plus depreciation.
  - C. cost to build new minus depreciation plus land.
  - D. sales price minus land and cost to build new plus depreciation.
28. An appraisal is used to determine which of the following?
- A. Probable sales price
  - B. Assessed value
  - C. List price
  - D. Market price
29. The subject property has five bedrooms and three-and-a-half bathrooms. Which of the following comparables would require a deduction from the sales price?
- A. Comparable 1 has four bedrooms and three bathrooms.
  - B. Comparable 2 has no air-conditioning or fireplace.
  - C. Comparable 3 is in a better condition.
  - D. Comparable 4 has the same square footage but no patio.
30. The monthly gross rent multiplier is 100, and the annual rent is \$12,000. What is the estimated value?
- A. \$12,000
  - B. \$100,000
  - C. \$120,000
  - D. \$1,200,000
  - E. None of these

# UNIT 16 BROKER-LEVEL QUESTIONS

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1. In an area where rental rates have been at historic highs, the rates have started to drop. The principle of value that would explain this change is
  - A. substitution.
  - B. sales comparison.
  - C. supply and demand.
  - D. anticipation.
2. A broker has been asked to do a CMA on a four-unit rental. What is the first step the broker should take?
  - A. Choose which comparables to use
  - B. Determine the gross, effective, and net operating incomes
  - C. Decide whether to price the property using the reproduction or replacement value
  - D. Estimate the value of the land using the market data approach
3. An appraiser used all three approaches to value and found the following values for a small four-unit rental property: sales comparison approach value was \$450,000; cost approach value was \$500,000; and income approach value was \$425,000. How would the appraiser determine the value of the property?
  - A. Add the three values and divide by three to determine the overall value
  - B. Give the sales comparison approach the most weight because it is in the middle
  - C. Use the value determined by the cost approach because it is the highest
  - D. Give the income approach the most weight because the property is a rental
4. In question 3, which approach would have the MOST weight if the property were a single-family home?
  - A. Sales comparison approach
  - B. Cost approach
  - C. Income approach
  - D. Gross rent multiplier



# UNIT 16 QUIZ ANSWERS

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1. **A** The answer is sales comparison approach. The sales comparison approach is the most important approach for the appraisal of single-family residences.
2. **C** The answer is 9%. The net operating income (\$18,000) divided by the value (\$200,000) equals a rate of return of 0.09 or 9%.
3. **C** The answer is cost approach. The cost approach estimates the replacement cost, subtracts depreciation from all sources, and adds the value of the land to arrive at an estimate of value.
4. **A** The answer is functional obsolescence. Inadequate design or equipment is functional obsolescence.
5. **A** The answer is neighborhood decline. A declining neighborhood is an example of external/economic obsolescence.
6. **A** The answer is the current cost to rebuild with the same or highly similar materials. Reproduction cost is the cost of building a replica.
7. **C** The answer is a church. The cost approach is most often used for unique or special-purpose properties (e.g., churches and schools).
8. **C** The answer is an apartment building. Income capitalization (the income approach to value) is used to appraise income-producing properties (e.g., office buildings, shopping centers, and apartment buildings).
9. **D** The answer is capitalization. Capitalization is part of the income approach, which does not include adjustments to comparables.
10. **A** The answer is present value based on current or expected income. Capitalization is the process by which present value is estimated based on expected income.
11. **B** The answer is substitution. The principle of substitution states that buyers would not pay more for a property than they would have to pay to acquire a similar substitute property.
12. **B** The answer is 7.6%.  $\$27,000$  (gross income)  $\times$  45% or 0.45 (expenses) = \$12,150 expenses.  
 $\text{gross income} - \text{expenses} = \text{net income}$   
 $\$27,000 - \$12,150 = \$14,850$   
 $\text{net income} \div \text{property value} = \text{cap rate}$   
 $\$14,850 \div \$195,000 = 0.076$  or 7.6% cap rate
13. **A** The answer is has the same function and utility. Replacement cost new is the present cost of replacing the subject improvement with another that has the same function and utility, using current construction standards and costs.
14. **A** The answer is the opinion is not an appraisal. A salesperson completing a BPO may be paid but must make sure the receiver (in this case, the bank) knows the opinion is not an appraisal.
15. **C** The answer is the sales prices of the comparables should be adjusted downward. Adjustments are always made to the comparables. If the comparable is superior to the subject, the sales price of the comparable is adjusted downward.
16. **C** The answer is cost approach. In the cost approach, the appraiser must estimate the accrued depreciation to be subtracted from the replacement cost of the improvements.
17. **C** The answer is sales price and rental rates. Divide the sales price by the rental rates to determine the gross rent multiplier.
18. **D** The answer is profitability. The essential elements of value are demand, utility, scarcity, and transferability (DUST).

19. **C** The answer is the price will likely increase. When demand increases, it causes prices to increase.
20. **C** The answer is reconciliation. In reconciliation, the appraiser uses professional judgment to weigh the alternative values and estimate the best value for the subject property.
21. **A** The answer is conformity. Conformity uses progression and regression.
22. **A** The answer is cost approach. Depreciation is used in the cost approach to value.
23. **C** The answer is sales comparison approach. Comparables are used in the market data or sales comparison approach.
24. **D** The answer is contribution. Contribution through increasing and decreasing returns will reveal whether upgrades will add more value than they cost.
25. **D** The answer is the most probable price. Market value is the most probable price a property will bring. Market price is the actual sales price.
26. **B** The answer is \$240,000. To determine value, the monthly GRM is multiplied by the income, which must be converted to a monthly figure:  
$$120 \times (\$24,000 \div 12) = \$240,000.$$
27. **C** The answer is cost to build new minus depreciation plus land. The formula used in the cost approach is the cost to build new minus depreciation plus land.
28. **A** The answer is probable sales price. An appraisal estimates market value, which is the probable sales price that a property will bring in an open market.

29. **C** The answer is comparable 3 is in a better condition. The condition of comparable 3 is better than the subject, so it needs to be adjusted downward to make it similar to the subject. The other comparables would need to be adjusted upward.
30. **B** The answer is \$100,000. Match the multiplier and convert to monthly rent.  
$$\$12,000 \text{ per year} \div 12 \text{ months} = \$1,000 \text{ per month.}$$
$$\$1,000 \text{ monthly rent} \times 100 \text{ MGM} = \$100,000.$$

### Broker-Level Questions

1. **C** The answer is supply and demand. The principle of supply and demand would predict whether the fall in rental rates is due to more supply or less demand in the market.
2. **B** The answer is determine the gross, effective, and net operating incomes. The broker would use the income approach because the property is income producing and the broker needs the NOI to calculate the value.
3. **D** The answer is give the income approach the most weight because the property is a rental. The most weight would be given to the income approach because the property is a rental. Averaging is never used in any phase of the appraisal process.
4. **A** The answer is the sales comparison approach has the most weight when appraising a single-family home.

# UNIT 17

## Leases

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain the essential elements of leasehold interests.
- › Describe the essential terms of a lease agreement.
- › Distinguish the various types of leases.
- › Explain the means by which the lease may be terminated and discharged and the remedies available to the parties for its breach.

### KEY POINTS—UNIT 17

- A lease is a bilateral contract in which the property owner promises to allow the tenant to possess the owner's property and the tenant promises to pay rent.
- The owner of leased property is referred to as the lessor; the tenant is the lessee.
- When under lease, the owner of real estate holds a leased fee estate. The tenant has a leasehold estate. The owner/lessor has a reversionary interest, meaning the owner will retake possession when the lease terminates.
- In a gross lease, the tenant pays rent plus expenses directly to the landlord, who then pays all expenses for the building.
- In a net lease, the tenant pays a base rent to the landlord, but the tenant is responsible for paying property expenses, including property taxes, insurance, maintenance, repairs, and so on. Expenses do not include the owner's mortgage payment.
- A percentage lease may be used for retail property. The tenant pays a base rent plus a percentage of gross sales over an amount agreed on in the lease.
- A graduated lease increases rents by a predetermined amount at predetermined intervals, typically annually.

- The amount of rent paid in an index lease will vary based on an agreed-on index, such as the Consumer Price Index.
- The lessee rents just the ground in a land lease (ground lease), which is typically a long-term lease of 55–99 years. Any improvements built by the tenant will become the property of the landlord upon lease termination, unless otherwise agreed to in the lease.
- There are four types of leasehold estates: estate for years, estate from period to period (periodic tenancy), estate at will, and estate at sufferance.
- An estate for years has a predetermined termination date written into the lease. No notice is required to terminate the lease. Death of the landlord or tenant does not terminate the lease.
- A periodic estate is a lease for a specific term, usually month to month, that automatically renews when the landlord accepts rent from the tenant. Notice is required to terminate the lease.
- An estate at will has no agreed-on duration. The tenant occupies space at the will, or permission, of the owner. Death or notice terminates an estate at will.
- An estate at sufferance occurs when the leasehold has terminated but the tenant remains in possession of the property.
- An eviction is a court action brought by the landlord against a tenant who is in breach of the lease, often nonpayment of rent. A constructive eviction is brought by the tenant to terminate the lease due to the landlord's actions or inactions. Constructive eviction would occur, for instance, if the landlord fails to pay the water bill, resulting in the water being shut off.

## I. LEASING REAL ESTATE

### A. Overview

1. The lease is the foundation of the relationship of property owner and tenant.
2. The \_\_\_\_\_ is the owner of the real estate, also called the landlord.
3. The \_\_\_\_\_ is the tenant.
4. The landlord retains a \_\_\_\_\_ to possession of the property after the lease term expires.
5. The \_\_\_\_\_ in most states requires lease agreements for more than one year to be in writing to be enforceable.

### B. Leasehold estates

1. Tenant's right to possess the real estate for the term of the lease is called a leasehold estate or \_\_\_\_\_ estate.
2. In an \_\_\_\_\_, the leasehold estate continues for a definite period.
3. In an \_\_\_\_\_, the lease agreement has an initial term, but will run for the same term for an indefinite time until proper notice of \_\_\_\_\_ is given.
  - a. In a month-to-month tenancy, there is no definite termination date but the tenant \_\_\_\_\_.
  - b. If the tenant remains on the premises after a lease expires, a \_\_\_\_\_ may be created.

4. In an \_\_\_\_\_, the tenant has the right to possess property with the landlord's consent for an unspecified or uncertain term.
5. In an \_\_\_\_\_, a tenant who lawfully took possession of real property continues in possession without the landlord's consent.

## II. LEASE AGREEMENTS

### A. Requirements of a valid lease

1. Parties must have \_\_\_\_\_.
2. The lease must have a \_\_\_\_\_.
3. There must be an offer and acceptance, also called a \_\_\_\_\_.
4. The lease must be supported by \_\_\_\_\_, an exchange of promises.

### B. Possession of premises

1. The lessor owes the lessee the covenant of \_\_\_\_\_ of the premises.
2. Except in emergencies, before entering leased premises, the landlord must give the tenant \_\_\_\_\_.
3. A lessor may restrict a lessee's use of the premises through provisions \_\_\_\_\_ in the lease.

### C. Term of lease

1. The length of the lease should be stated precisely, including \_\_\_\_\_ dates.
2. Some states prohibit leases that run for 100 years or more.

### D. Security deposit

1. Tenants are often required to provide a \_\_\_\_\_ that is held by the landlord during the lease term.
2. State law may regulate the amount and purpose of any security deposit.

### E. Improvements

1. Neither landlord nor tenant is required to make improvements to leased property.
2. The tenant may make improvements with the landlord's permission or as required to make the rented premises \_\_\_\_\_.

**F. Accessibility**

1. Federal and state fair housing laws make it illegal to discriminate against a prospective tenant on the basis of the tenant's \_\_\_\_\_.
2. The tenant must be permitted to make \_\_\_\_\_ to a property at the tenant's own expense.
3. The Americans with Disabilities Act (ADA) affects a landlord's obligation when a commercial property or place of public accommodation is leased.

**G. Maintenance of premises**

1. A lessor of residential property usually is required by state law to maintain dwelling units in a \_\_\_\_\_.
2. Residential tenants do not have to make repairs, but must \_\_\_\_\_ in the same condition they were received, allowing for ordinary wear and tear.
3. A lessee of commercial or industrial property usually maintains the premises and is often responsible for making their own repairs.

**H. Destruction of premises**

1. The obligation to pay rent for damaged or destroyed premises depends on the \_\_\_\_\_ and the lease.
2. Tenants who construct buildings on leased land are still obligated for payment of rent even if the improvements are \_\_\_\_\_.

**I. Assignment and subleasing**

1. In an assignment of a lease, a tenant transfers the entire \_\_\_\_\_ to another person.
2. Under a sublease, a tenant transfers \_\_\_\_\_ the entire leasehold interest by subletting the premises to a new tenant.

**J. Recording a lease**

1. Most leases are not recorded because the inspection of leased property provides \_\_\_\_\_ of the tenant's occupancy.
2. Some states require the recording of a long-term lease, particularly when the leasehold interest is \_\_\_\_\_.

**K. Options**

1. A \_\_\_\_\_ in a lease gives the lessee the privilege of renewing the lease, but the lessee must give notice of intent to exercise the option.
2. A \_\_\_\_\_ gives the lessee the right (but not the obligation) to purchase the leased property.
3. The lease option could give the tenant the \_\_\_\_\_ that allows the tenant the opportunity to buy the property before the owner accepts an offer from another party.

**III. TYPES OF LEASES****A. Gross lease**

1. The tenant pays \_\_\_\_\_ to the landlord, who pays the expenses.
2. Most typical for residential, but could be used for commercial properties

**B. Net lease**

1. The tenant pays \_\_\_\_\_ (e.g., property taxes, insurance, maintenance).
2. Leases for entire commercial and industrial buildings and the land on which they are located, ground leases, and long-term leases are usually \_\_\_\_\_.

**C. Percentage lease**

1. Rent is a base rent plus a percentage of \_\_\_\_\_ received by the tenant.
2. Most common in retail properties

**D. Variable lease**

1. Rent increases or decreases at predetermined intervals.
2. In a graduated lease, rent increases at predetermined intervals at the amount set in the lease terms.
3. In an index lease, rent is adjusted based on an economic indicator, such as the Consumer Price Index.

**E. Other types of leases**

1. A ground lease may be used for \_\_\_\_\_.
  - a. Improvements become the \_\_\_\_\_ property at the end of the lease.
  - b. The tenant would want a \_\_\_\_\_ lease if adding improvements.

2. Oil and gas lease
  - a. Allows drilling on land
  - b. Usually provides a \_\_\_\_\_ to the landowner
3. A lease purchase will allow the tenant to \_\_\_\_\_ in the future.
4. Sale-and-leaseback frees up capital while allowing the original property owner to \_\_\_\_\_.

#### IV. DISCHARGE OF A LEASE

##### A. Contract terminates

1. The parties have fully \_\_\_\_\_.
2. The parties agree to \_\_\_\_\_ the lease.
3. By operation of law, as in a bankruptcy, foreclosure, or \_\_\_\_\_

##### B. Breach of lease

1. \_\_\_\_\_ is a court action brought by the landlord against a tenant who is in breach.
2. \_\_\_\_\_ eviction
  - a. A lease is \_\_\_\_\_ if the tenant must vacate due to the landlord's act or failure to act.
  - b. Cancels lease and tenant's obligation to pay rent, but the \_\_\_\_\_



## UNIT 17 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

accepts rent	gross lease	notice
actual eviction	index	percentage
advance notice	lessee	periodic estate
constructive eviction	lessor	specific
death	net lease	termination

1. A lease contract in which the tenant pays base rent plus expenses is a(n) \_\_\_\_\_.
2. A lease contract in which the tenant pays rent with no additional expenses is a(n) \_\_\_\_\_.
3. The landlord is the \_\_\_\_\_ and the tenant is the \_\_\_\_\_.
4. Sometimes used in retail properties, with a(n) \_\_\_\_\_ lease, the tenant typically pays a base rent plus percentage of gross sales over an agreed-on threshold.
5. A lease with a(n) \_\_\_\_\_ termination date is an estate for years, regardless of the length of the lease.
6. A lease with a rent payment that adjusts based on an economic indicator is a(n) \_\_\_\_\_ lease.
7. A month-to-month lease is a(n) \_\_\_\_\_, which renews when the landlord \_\_\_\_\_ for the period and may be terminated by \_\_\_\_\_ given by either party.
8. An estate for years and a periodic estate are not terminated by the \_\_\_\_\_ of the landlord or the tenant.
9. A landlord may pursue \_\_\_\_\_ through the courts to terminate a tenant's lease for nonpayment of rent.
10. A tenant may take legal action called \_\_\_\_\_ to terminate the lease because of the landlord's breach of contract.

## UNIT 17 GLOSSARY REVIEW ANSWERS

1. net lease
2. gross lease
3. lessor, lessee
4. percentage
5. specific
6. index
7. periodic estate, accepts rent, advance notice
8. death
9. actual eviction
10. constructive eviction

# UNIT 17 QUIZ

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1. A contract that conveys the right to possess and use property but does NOT convey title is
  - A. a bill of sale.
  - B. a lease.
  - C. a quitclaim deed.
  - D. a dedication.
2. A commercial lease in which the tenant pays the landlord a base rent plus a share of the gross sales from the tenant's business is
  - A. a net lease.
  - B. a ground lease.
  - C. a gross lease.
  - D. a percentage lease.
3. A lease in which the tenant pays a base rent plus a portion of the property's operating expenses is
  - A. a percentage lease.
  - B. a net lease.
  - C. a gross lease.
  - D. a standard lease.
4. A landlord has not paid the utility bills for his apartment building, so the heat, water, and electricity are shut off. Because of this, the tenants may have the right to terminate their leases and move out of the building. Which of the following legal concepts does this example illustrate?
  - A. Constructive eviction
  - B. Mutual rescission
  - C. Actual eviction
  - D. Eminent domain
5. A tenant holds an estate for years, but has stopped paying rent and therefore breached the lease contract. What legal action may the landlord use to remove the tenant?
  - A. Constructive eviction
  - B. Unilateral rescission
  - C. Actual eviction
  - D. Advance notice
6. Your lease expires at midnight on January 12. What type of leasehold estate do you have?
  - A. Periodic estate
  - B. Estate at will
  - C. Estate at sufferance
  - D. Estate for years
7. When you ask your friends how much rent they pay for their commercial space, they respond, "\$3,500 per month gross." Which statement is likely to be the MOST accurate?
  - A. The rent includes all utilities and expenses.
  - B. They bought the space on a contract for deed.
  - C. The lease includes an outdoor storage yard.
  - D. The rent does not include utilities or expenses.
8. A lease is a contract between the lessor and lessee in which
  - A. the tenant has equitable title, and the landlord holds legal title.
  - B. the tenant has possession and holds legal title.
  - C. the tenant has legal possession of the property.
  - D. the landlord has possession of the property.
9. Which of the following would terminate a periodic estate, such as a month-to-month lease?
  - A. Reaching the termination date
  - B. Advance notice by either party
  - C. Death of the landlord or tenant
  - D. All of these

# UNIT 17 QUIZ ANSWERS

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1. **B** The answer is a lease. The lessor (landlord) grants the right of possession to the lessee (tenant); the lessor retains title.
2. **D** The answer is a percentage lease. Percentage leases are used in commercial and retail properties.
3. **B** The answer is a net lease. In a net lease, the tenant pays a base rent plus some or all of the operating expenses associated with the tenant's space.
4. **A** The answer is constructive eviction. In a constructive eviction, the tenant takes legal action to terminate the lease because the landlord has caused or permitted a substantial interference with the tenant's use and enjoyment of the property.
5. **C** The answer is actual eviction. Actual eviction is a court action brought by the landlord against a tenant who is in breach.
6. **D** The answer is estate for years. The tenant holds an estate for years if the lease contains a specific termination date.
7. **A** The answer is the rent includes all utilities and expenses. A tenant pays gross rent in a gross lease. The gross rent payment includes the base rent plus the tenant's share of utilities.
8. **C** The answer is the tenant has legal possession of the property. The lessor/landlord has reversionary interest, allowing the landlord to retake possession at lease termination.
9. **B** The answer is advance notice by either party. A periodic estate, such as a month-to-month lease, is terminated by either party providing advance notice of their intent to terminate the lease. The amount of notice is determined by the lease or state law.

# UNIT 18

## Fair Housing

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain the significance of the Civil Rights Act of 1866 to equal opportunity in housing.
- › Describe the various federal laws that protect Americans from unfair housing practices.
- › Describe blockbusting, steering, redlining, and other abusive housing practices.
- › List the various recourses available to the aggrieved person who believes illegal discrimination has occurred, including acts of real estate professionals.

### KEY POINTS—UNIT 18

- There are local, state, and federal civil rights and fair housing laws that prohibit discrimination in real estate transactions. The earliest federal law is the Civil Rights Act of 1866, which prohibits discrimination based on race or color in any property transaction.
- The federal Fair Housing Act of 1968 prohibits discrimination based on race, color, religion, sex, national origin, handicap, or familial status in transactions involving housing or vacant land intended to be used for residential purposes. There are several exemptions from the Fair Housing Act, but the exemptions do not allow discrimination based on race or color because of the Civil Rights Act of 1866. The exemptions do not apply to any transactions in which a real estate professional is employed.
- Three practices specifically prohibited under the Fair Housing Act are steering, redlining, and blockbusting. Steering is channeling buyers or renters to or away from specific neighborhoods based on protected class characteristics. Redlining is refusing to make loans on properties located in particular areas for discriminatory reasons, such as the ethnicity of residents. Blockbusting (panic selling) is attempting to obtain listings or arrange sales by predicting the entry of certain groups into a neighborhood and representing that this will cause a decline in property values in the neighborhood.

- The Americans with Disabilities Act (ADA) is intended to ensure equal access to public accommodations for persons with a disability. The law requires entities with facilities open to the public to eliminate architectural and communication barriers to access the facilities and to provide auxiliary aids and services for persons with a disability.
- Real estate professionals, property sellers, and landlords must also comply with state and local fair housing and accessibility laws, which may have more requirements than federal law.

## I. EQUAL OPPORTUNITY IN HOUSING

### A. Civil Rights Act of 1866

1. Prohibits discrimination in the sale and rental of property based on race, with no exceptions
2. United States Supreme Court cases and other laws followed in the next century
  - a. In 1896, *Plessy v. Ferguson* resulted in the \_\_\_\_\_ doctrine.
  - b. In 1941, President Franklin Delano Roosevelt's executive order prohibited racial discrimination in the \_\_\_\_\_.
  - c. In 1954, the Supreme Court overturned *Plessy* with the decision in *Brown v. Board of Education*, holding that separate schools for black and white students were \_\_\_\_\_.
  - d. The Civil Rights Act of 1957 protects the \_\_\_\_\_ of African Americans.

### B. Fair Housing Act/Civil Rights Act of 1968

1. Prohibits discrimination in the sale, lease, appraisal, and financing of property based on the following protected classifications:
  - a. Race
  - b. Religion
  - c. Color
  - d. Sex
  - e. National origin
  - f. Familial status
    - i. Added in 1988
      - Protects families with \_\_\_\_\_ under the age of 18 and includes pregnant women and those fighting for child custody
    - ii. A landlord may refuse to rent to a family based on housing regulations (e.g., regulations may limit the number of occupants per bedroom).
    - iii. Congress passed the Housing for Older Persons Act (HOPA) in 1995 to permit housing intended for those \_\_\_\_\_.

- g. Disability
- i. Added in 1988 and protects those with physical or mental impairments, HIV/AIDS, and addiction
2. Exemptions
- a. Real estate licensees may not discriminate \_\_\_\_\_.
- b. All advertising must be in compliance with the law; there are no exemptions.
- i. \_\_\_\_\_ used to advertise housing, including online blogs and social media, fall under this rule.
- c. Unless prohibited by state or local law, discrimination is allowed based on religion, color, sex, national origin, familial status, or handicap/disability in the following situations:
- i. Rental or sale of a single-family home by the owner (\_\_\_\_\_)
- No real estate professional may take part in the transaction.
  - No discriminatory advertising
- ii. Rental of units in a one-to-four-unit building where the owner occupies one of the units
- No exemption for buildings with more than four units, even if the owner or owner's family occupies a unit
  - No real estate professional may take part in the transaction; no discriminatory advertising
- iii. Private clubs, not open to the public, may restrict lodgings to members only.
- iv. Religious organizations may give preference to their members for residential housing. The religion or denomination must not limit membership based on race, color, or national origin.
- v. \_\_\_\_\_
- At least \_\_\_\_\_ of the units are occupied by at least one person aged \_\_\_\_\_ or older
  - Allowed to refuse occupancy in rental or sale of units to families with children
3. Prohibitions
- a. If asked by the seller or buyer to discriminate, the licensee should cancel agency.
- b. It is a violation of the federal Fair Housing Act to do any of the following related to housing accommodations (residential property) based on membership in a protected class:
- i. Refuse to show, rent, sell, negotiate, or deal
- ii. Offer different terms

- iii. Advertise in a discriminatory fashion, including ads in newspapers, social media, and other online sites
  - May not advertise against any protected class
    - Unacceptable example: “no children” or “no Caucasians”
    - Acceptable example: “no smoking”
  - Acceptable to advertise in local neighborhood newspapers or websites that may cater to a protected class, as long as no preferential language is used
  - Advertise the property, not who should occupy it
- iv. Steering —\_\_\_\_\_ potential buyers to or away from particular areas as a means of discrimination
- v. \_\_\_\_\_—also called \_\_\_\_\_
  - Example: suggesting neighbors should sell because a member of a protected class has moved into the area
- vi. \_\_\_\_\_—refusing to offer or limiting loans in certain areas because of crime rates or the characteristics of the residents

#### 4. Americans with Disabilities Act (ADA)

- a. The ADA is intended to ensure equal access to public accommodations for a person with a disability.
- b. A public accommodation is any private entity with facilities \_\_\_\_\_, such as a real estate office.
- c. The ADA requires removal of architectural and communication barriers and provision of auxiliary aids and services, if readily achievable.
- d. New commercial and multifamily construction must be accessible to persons with a disability.
- e. A residential tenant with a disability may make property modifications \_\_\_\_\_. The unit must be returned to its original condition.
- f. Disability defined
  - i. A disability is any physical or mental impairment that substantially limits one or more major \_\_\_\_\_.
    - Includes HIV and AIDS
    - Those addicted to drugs or alcohol are protected in certain situations.
      - Those seeking treatment for addiction are protected—they may use controlled substances if prescribed by a doctor.
      - The illegal use of a controlled substance is not protected.



- The law specifically excludes those convicted of illegally distributing controlled substances.
- May discriminate based on criminal record
- Both current and recovered psychological patients are protected.

#### 5. Property management issues

- a. Landlords must allow a tenant with a disability to make changes to a unit.
  - i. The tenant must return the unit to its original state.
  - ii. Landlords \_\_\_\_\_ an extra damage deposit.
  - iii. Landlords may not deny tenancy, charge additional rent, or require a pet deposit for a service animal.
  - iv. Landlords are not required to rent to a tenant with a disability who has a criminal background.

#### 6. Complaints

- a. Complaints may be filed with federal or state authorities.
- b. At the federal level, a complaint must be filed with HUD within one year of the alleged discrimination.
- c. Complaints can be filed directly in federal court within \_\_\_\_\_.
  - i. HUD or the state will \_\_\_\_\_ the complaint.
  - ii. HUD will consider the following:
    - Conducting test scenarios to determine if the discrimination is repeated
    - The properties shown to the buyer or the tenant
    - If an equal opportunity poster is displayed in the broker's office
- d. HUD does not consider the intentions of the licensee even if the agent believed they were working in the consumer's best interest.

#### 7. Penalties

- a. May include injunctions, damages, court costs, attorney's fees, and civil penalties
- b. No imprisonment; not a criminal offense
- c. HUD, FHA, or VA may not revoke a real estate license.

8. The broker must display the equal opportunity poster.
  - a. The poster must be in each office or place of business.
  - b. Failure to display the poster can shift burden of proof to the broker in an alleged discrimination complaint.
  - c. The equal housing logo must be used in most advertising.
9. Protect against claims of discrimination by \_\_\_\_\_ (e.g., all showings, disclosures)

## UNIT 18 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

55 or older	Department of Housing and	original condition
80%	Urban Development (HUD)	real estate
Americans with Disabilities Act (ADA)	exempt	redlining
blockbusting	Fair Housing Act	steering
Civil Rights Act of 1866	familial status	strictest
	make modifications	

1. If there is a conflict among local, state, or federal fair housing laws, the \_\_\_\_\_ rule will apply.
2. Channeling buyers to or away from particular neighborhoods based on the buyer's ethnic background is an illegal practice called \_\_\_\_\_.
3. Lenders who define an area in which they will not originate loans based on the racial or ethnic characteristics of the residents in the area are \_\_\_\_\_.
4. Alleged incidents of discrimination can be reported to the \_\_\_\_\_, which will investigate the allegation.
5. Senior housing communities are allowed to discriminate based on \_\_\_\_\_ if at least \_\_\_\_\_ of the units are occupied by a person \_\_\_\_\_.
6. The \_\_\_\_\_ prohibits discrimination based on race, with no exceptions.
7. A real estate licensee advertising for listings by stating the "neighborhood is changing" may be in violation of the Fair Housing Act's prohibition against \_\_\_\_\_.
8. A federal law intended to ensure persons with a disability have equal access to public accommodations is the \_\_\_\_\_.
9. The federal law that prohibits housing discrimination based on race, color, national origin, religion, sex, familial status, or disability is the \_\_\_\_\_.
10. An owner-occupant leasing apartments in his four-unit building is \_\_\_\_\_ from the Fair Housing Act.
11. Regardless of directions from the client, \_\_\_\_\_ professionals may never discriminate.
12. Landlords must allow a person with a disability to \_\_\_\_\_ to property as long as the individual agrees to return the property to its \_\_\_\_\_ at their expense upon termination of the lease.

## UNIT 18 GLOSSARY REVIEW ANSWERS

1. strictest
2. steering
3. redlining
4. Department of Housing and Urban Development (HUD)
5. familial status, 80%, 55 or older
6. Civil Rights Act of 1866
7. blockbusting
8. Americans with Disabilities Act (ADA)
9. Fair Housing Act
10. exempt
11. real estate
12. make modifications, original condition

# UNIT 18 QUIZ

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1. If principals insist that they will not sell their house to members of a certain ethnic group, the agent must
  - A. obey the request, in accordance with the law of agency.
  - B. report the seller to the police.
  - C. refuse to honor the request.
  - D. obey the request but decline a commission.
2. The Fair Housing Act provides for exemptions from compliance in certain circumstances. The act allows an exemption for
  - A. a church-owned apartment complex if language in the lease restricts tenancy to members of a specific national origin.
  - B. a commercial restaurant and lounge owned by a private club that refuses to admit individuals of a certain ethnic group.
  - C. the absentee owner of a four-unit building who charges a higher rent to members of a certain religious group.
  - D. leasing to a large family if local housing regulations do not allow that number of occupants.
3. Which of the following is TRUE about a renter of a single-family home who has recently become disabled?
  - A. The tenant may build a ramp at the tenant's expense.
  - B. The landlord must build a ramp at the landlord's expense.
  - C. The tenant must vacate the premises within 30 days.
  - D. The landlord must reduce the tenant's rent.
4. Is it acceptable for an apartment building to advertise its apartments "for adults only"?
  - A. No, because it is illegal and discriminates against families with children
  - B. Yes, if each unit is occupied by at least one person age 55 or over
  - C. Yes, it is legal per federal, state, and local laws
  - D. No, it is illegal because fair housing laws protect age
5. Which of the following is NOT a protected group under federal fair housing laws?
  - A. Sex
  - B. Age
  - C. Race
  - D. Disability
6. Parties who believe they have suffered from housing discrimination may file a complaint in federal court within
  - A. 90 days from the incident.
  - B. 2 years from the incident.
  - C. 10 years from the incident.
  - D. a reasonable time.
7. A real estate salesperson is representing a couple who just arrived from Russia. The salesperson shows them only homes that are in neighborhoods with Russian immigrants and Russian-speaking merchants and services. This is
  - A. thoughtful.
  - B. blockbusting.
  - C. steering.
  - D. redlining.
8. If HUD believes fair housing law has been violated, which would be the first action taken?
  - A. Wait until at least one more incident is reported
  - B. File a lawsuit
  - C. Take the broker's license
  - D. Start an investigation
9. Owners and managers of qualified senior housing are allowed to discriminate based on
  - A. age.
  - B. religion.
  - C. familial status.
  - D. national origin.
10. A lender refusing to lend in an area of high crime rates might be guilty of
  - A. theft.
  - B. blockbusting.
  - C. steering.
  - D. redlining.

11. In renting residential units, a property manager may legally
  - A. refuse to rent a one-bedroom unit to a pregnant woman.
  - B. designate adults-only floors as long as there are floors for families.
  - C. charge a person with a disability a higher security deposit than other renters.
  - D. require a person with a disability who made alterations to restore the property to its original condition upon lease termination.
12. Which of the following is a protected classification under the federal Fair Housing Act?
  - A. Addiction
  - B. Marital status
  - C. Sexual orientation
  - D. Legal source of income
13. Which of the following is NOT exempt from the federal Fair Housing Act?
  - A. An owner-occupant leasing apartments in a four-unit building
  - B. A seller selling her own home
  - C. A senior housing facility excluding families with children
  - D. A real estate licensee hired to lease vacant apartments
14. An agent soliciting listings in a neighborhood by suggesting homeowners should sell due to a recent change in the race or ethnicity of the area may be practicing illegal
  - A. redlining.
  - B. blockbusting.
  - C. steering.
  - D. commingling.
15. Which of the following is protected by the Civil Rights Act of 1866 and the Fair Housing Act of 1968?
  - A. Religion
  - B. Color
  - C. Race
  - D. National origin
16. A federal law intended to ensure disabled persons equal access to public accommodations is
  - A. the Americans with Disabilities Act (ADA).
  - B. the Fair Housing Act.
  - C. the Civil Rights Act.
  - D. the Equal Credit Opportunity Act (ECOA).
17. Which of the following is NOT considered a handicap and is unprotected under the Americans with Disabilities Act (ADA)?
  - A. Treatment for addiction
  - B. Illegal use of a controlled substance
  - C. Medically prescribed use of a controlled substance
  - D. None of these are protected

# UNIT 18 BROKER-LEVEL QUESTIONS

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1. An agent lives and specializes in a neighborhood with a mostly Hispanic population. The agent just listed a property in the neighborhood and agreed to advertise it with a local Spanish language newspaper and social media site. Are these ads acceptable?
  - A. Yes, as long as they do not use preferential descriptions, such as “enjoy this Hispanic neighborhood”
  - B. No, unless he also places the same ads in other neighborhood papers and social media sites that have different demographics
  - C. Yes, if the ads are in both English and Spanish
  - D. No, because this is considered steering

# UNIT 18 QUIZ ANSWERS

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1. **C** The answer is refuse to honor the request. An agent is not required to and cannot break the law at the request of a client. The agent must not discriminate. A listing contract with an illegal purpose is void.
2. **D** The answer is leasing to a large family if local housing regulations do not allow that number of occupants. A landlord may refuse to rent to families based on occupancy requirements in local housing ordinances.
3. **A** The answer is the tenant may build a ramp at the tenant's expense. The tenant must be allowed to make changes to the property at the tenant's expense. The landlord may require the tenant to return the property to its original condition upon lease termination.
4. **B** The answer is yes, if each unit is occupied by at least one person age 55 or over. Approved senior housing in which 80% of the units are occupied by at least one person age 55 or over may discriminate against families with children.
5. **B** The answer is age. Age is not a federal fair housing protected class, but age is a protected category under the Equal Credit Opportunity Act (ECOA).
6. **B** The answer is two years from the incident. Complaints regarding housing discrimination may be filed within two years in federal court.
7. **C** The answer is steering. Selecting properties to show based on any protected class (national origin) is prohibited. This channeling is called steering. The client may ask to be shown homes in certain areas, but the agent may not steer the client.
8. **D** The answer is start an investigation. Once a complaint has been found to be legitimate, HUD will start an investigation.
9. **C** The answer is familial status. Qualified senior housing is allowed to discriminate against families with dependent children under age 18 (familial status).
10. **D** The answer is redlining. There is no legal redlining. Lenders are not allowed to refuse to lend based on crime rates in an area. Loans are based on the applicant's financial qualifications.
11. **D** The answer is require a person with a disability who made alterations to restore the property to its original condition upon lease termination. The tenant must be allowed to make changes, and the landlord may require that the property be returned to its original condition upon lease termination. Pregnant women and individuals with children are covered under the familial status category.
12. **A** The answer is addiction. Addiction is considered a disability and protected.
13. **D** The answer is a real estate licensee hired to lease vacant apartments. Real estate licensees are not exempt from the Fair Housing Act under any circumstances.
14. **B** The answer is blockbusting. Panic selling (blockbusting) is the illegal practice of inducing owners to sell by claiming property values will decline based on the arrival of residents of a particular race, religion, color, sex, national origin, familial status, handicap, or disability.
15. **C** The answer is race. The Civil Rights Act of 1866 prohibited discrimination based on race. The 1968 Fair Housing Act added religion, color, and national origin. Disability and familial status were protections added in 1988.
16. **A** The answer is the Americans with Disabilities Act (ADA). The ADA goes beyond housing discrimination and is intended to provide equal access to any venue the general public has access to.



17. **B** The answer is illegal use of a controlled substance. Housing can be denied to those illegally using a controlled substance. Those using a controlled substance such as prescription painkillers prescribed by a medical professional are protected.

### Broker-Level Questions

1. **A** The answer is yes, as long as they do not use preferential descriptions, such as “enjoy this Hispanic neighborhood.” The broker may advertise in the local Spanish language newspaper and social media site as long as the broker does not use any language that would exclude others or show a preference for one group over another.



# UNIT 19

## Property Management

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Describe the various property management assignments available in the property management field and the role of the property manager in each.
- › Explain the essential elements of the property management agreement.
- › List the primary responsibilities of the property manager.
- › Describe the various federal laws, which the property manager must know and follow in the performance of management.
- › Describe the implementation of risk management procedures to ensure the safety and security of a managed property's tenants, as well as to protect the landlord from liability and loss.

### KEY POINTS—UNIT 19

- Risk management is the process used to assess risk and decide whether it is better to avoid, control, transfer, or retain the risk.
- A property manager must be a licensed real estate broker. Sales associates may not individually enter into management agreements.
- A property management agreement is a contract between the owner of an income-producing property and a brokerage firm that will act as the property manager.
- Property managers are responsible for the financial, physical, and administrative management of rental properties of all types.
- Duties include marketing vacant space, processing rental applications, negotiating leases, collecting rents, and complying with rent control rules and fair housing laws.
- Property managers develop budgets and prepare financial reports for building owners. The manager will include a reserve for replacement, which is monies set aside for the replacement of short-life items, such as air conditioners, appliances, carpeting, and so on.

- The property manager would have the authority to clean and paint vacant units, but would not have the authority to construct capital improvements, such as a total renovation of the unit.
- Brokers managing industrial or manufacturing properties should be cognizant of environmental issues.

## I. THE PROPERTY MANAGER

### A. Goals of the property manager

1. Achieve the objectives of the \_\_\_\_\_
2. Generate \_\_\_\_\_ for the owners
3. Preserve and/or increase the \_\_\_\_\_

### B. Securing management business

1. Possible clients of a property manager include
  - a. Property \_\_\_\_\_
  - b. Homeowners \_\_\_\_\_
  - c. Investment \_\_\_\_\_
  - d. Trusts
2. Areas of specialization for property managers include the following:
  - a. Community association management
  - b. Housing for \_\_\_\_\_
  - c. Manufactured homes
  - d. Resort housing
  - e. Concierge services
  - f. Asset \_\_\_\_\_
  - g. Corporate \_\_\_\_\_
  - h. Leasing \_\_\_\_\_
3. Professional associations provide information and contacts for all aspects of property management.

## II. THE MANAGEMENT AGREEMENT

### A. Key points

1. A property management agreement is a contract between the owner of an income-producing property and a brokerage firm that will act as the property manager. Their agreement should include
  - a. a description of the \_\_\_\_\_;
  - b. the time period the agreement covers and specific provisions for \_\_\_\_\_;
  - c. a definition of the manager's \_\_\_\_\_; and
  - d. a statement of the owner's purpose and responsibilities.
2. Parties to the contract
  - a. Property owner— \_\_\_\_\_
  - b. Property manager (brokerage firm)— \_\_\_\_\_
3. The manager's responsibilities in the contract are financial, physical, and administrative management to do the following:
  - a. \_\_\_\_\_ of the property
  - b. \_\_\_\_\_ from the property
  - c. Find well-qualified tenants
4. Management responsibilities include the following:
  - a. Marketing the space to attract tenants
  - b. Collecting rents and complying with rent control rules
  - c. Negotiating leases, including investigating applicants' qualifications
  - d. Developing a budget and preparing financial reports, including reserves for replacement of short-life items such as air conditioners, appliances, carpeting, and so on
  - e. Generating frequent, detailed reports on operations and finances
  - f. Compensation for the manager
  - g. Antitrust provisions
  - h. Equal opportunity statement

### III. THE PROPERTY MANAGER'S RESPONSIBILITIES

#### A. The management plan

#### B. Financial reports

1. Operating budget
2. Cash flow report
3. Income
4. Expenses
5. Cash flow
6. Profit and \_\_\_\_\_ statement
7. Budget \_\_\_\_\_ statement

#### C. Renting the property

1. Setting rental rates
2. Marketing
3. Advertising
4. Management activities
5. Marketing and advertising costs
6. Selecting \_\_\_\_\_
7. Collecting \_\_\_\_\_
8. Maintaining \_\_\_\_\_ with tenants

### IV. FEDERAL LAWS PROHIBITING DISCRIMINATION

#### A. Americans with Disabilities Act

1. Any employer of 15 or more employees must adopt nondiscriminatory \_\_\_\_\_.
2. The ADA prohibits discrimination in commercial properties and places of \_\_\_\_\_.

#### B. Equal Credit Opportunity Act

1. Property managers should use the \_\_\_\_\_ lease application for every applicant.
2. Managers should be consistent in evaluating the \_\_\_\_\_ of applicants.

**C. Fair Housing Act**

1. Federal fair housing laws prohibit discrimination in the sale, rental, or financing of housing based on a person's race, color, religion, national origin, sex, familial status, or disability.

**V. RISK MANAGEMENT****A. Techniques for evaluating risk**

1. \_\_\_\_\_ —by removing the source of risk (e.g., a swimming pool may pose an unacceptable risk)
2. \_\_\_\_\_ —by preparing for an emergency before it happens (e.g., installing sprinklers, fire doors, and security systems)
3. \_\_\_\_\_ —by shifting the risk to another party (e.g., taking out an insurance policy)
4. \_\_\_\_\_ —by deciding that the chances of the event occurring are too small to justify the expense of any response
5. Remember \_\_\_\_\_ (Act to Lessen Risk)

**B. Types of insurance**

1. Tenant's insurance
2. Commercial insurance
  - a. Fire and \_\_\_\_\_
  - b. Flood
  - c. Consequential loss, use, and occupancy
  - d. Contents and \_\_\_\_\_
  - e. \_\_\_\_\_ liability
  - f. Casualty
  - g. Surety \_\_\_\_\_

**C. Insurance claims**

1. Could be based on the depreciated or \_\_\_\_\_ of the property
2. Alternately, could be based on the current \_\_\_\_\_ of the property

## UNIT 19 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

avoid  
brokerage  
controlling  
environmental

general agency  
maintain value  
maintenance  
retain

sales associate  
transferring  
well-qualified tenants

1. The responsibilities of a property manager are to \_\_\_\_\_, generate income, and find \_\_\_\_\_.
2. Property management contracts are agreements between an income property owner and a real estate \_\_\_\_\_.
3. A property management agreement creates a(n) \_\_\_\_\_ between a real estate brokerage and the property owner.
4. A real estate \_\_\_\_\_ may enter into a property management agreement only on behalf of the sales associate's employing brokerage firm.
5. A property manager removing a source of risk, such as an outdoor playset, is taking a measure to \_\_\_\_\_ risk.
6. Installing a fence to limit access to a swimming pool is a means of \_\_\_\_\_ risk.
7. Buying an insurance policy is an example of \_\_\_\_\_ risk to another party.
8. A manager of a multifamily property may decide the chances of anyone stumbling on a little used pathway are too remote to justify the cost of repaving, thus deciding to \_\_\_\_\_ the risk.
9. Brokerages managing industrial and manufacturing facilities may have cause to be concerned about \_\_\_\_\_ issues, such as contaminated soils and flooring surfaces.



## UNIT 19 GLOSSARY REVIEW ANSWERS

1. maintain value, well-qualified tenants
2. brokerage
3. general agency
4. sales associate
5. avoid
6. controlling
7. transferring
8. retain
9. environmental

# UNIT 19 QUIZ

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1. A brokerage that requires all licensees to carry errors and omissions insurance is using which risk management technique?
  - A. Retaining the risk
  - B. Avoiding the risk
  - C. Controlling the risk
  - D. Transferring the risk
2. A property manager is BEST described as
  - A. a general agent.
  - B. a special agent.
  - C. a universal agent.
  - D. a facilitator.
3. The property manager's first obligation is to
  - A. maintain the value of the property.
  - B. earn a profit.
  - C. find high-quality tenants.
  - D. hire good contractors.
4. The contract that allows a property manager to screen tenants and collect rent is
  - A. a lease contract.
  - B. a gross lease.
  - C. a management contract.
  - D. a listing contract.
5. To manage rental property for another and for a fee, the property manager may be
  - A. a licensed sales associate.
  - B. a licensed real estate brokerage.
  - C. an unlicensed real property consultant.
  - D. all of these.
6. Which of the following would be an example of a property manager controlling risk?
  - A. Upgrading the fire and life safety systems
  - B. Demolishing the swimming pool
  - C. Purchasing a liability policy
  - D. Deciding a risk is too small to take action
7. A property manager decides to remove a makeshift treehouse from a wooded area at the edge of the apartment complex grounds. Which risk management technique is the property manager using by removing the source of the risk?
  - A. Control
  - B. Transfer
  - C. Avoid
  - D. Retain
8. An apartment complex offers its tenants various amenities, including a well-appointed party room. In front of the room's large-screen television, there's a sunken area, which is one step down from the rest of the floor space. A person could possibly trip or stumble there, although in 20 years, there have been no accidents. The property manager decides against installing a \$7,500 railing system along the step. Which of the following BEST describes this risk management strategy?
  - A. Retain the risk by deciding the chances of anyone stumbling are too small to justify the \$7,500 expense
  - B. Control the risk by preparing for an emergency before it happens (e.g., installing the railing system)
  - C. Transfer the risk by taking out an additional insurance policy
  - D. Avoid the risk by reconstructing the floor to remove the step

# UNIT 19 QUIZ ANSWERS

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1. **D** The answer is transferring the risk. The broker is transferring the risk to the insurance company.
2. **A** The answer is a general agent. A property manager is a general agent of the property owner. The relationship is an ongoing business enterprise that grants the property manager limited authority to contractually bind the property owner by signing leases on the owner's behalf.
3. **A** The answer is maintain the value of the property. The first obligation of a property manager is to maintain the value of property to protect the owner's investment. The manager would do this by finding well-qualified tenants and hiring reputable contractors.
4. **C** The answer is a management contract. The contract that gives property managers general agency obligations and allows them to screen tenants and collect rent is the management contract.
5. **B** The answer is a licensed real estate brokerage. Only a licensed real estate brokerage may manage property for another and for a fee.
6. **A** The answer is upgrading the fire and life safety systems. Taking action to better prepare for an emergency before it occurs is an example of controlling risk.
7. **C** The answer is avoid. A risk can be eliminated by removing (or not installing) the potential hazard.
8. **A** The answer is retain the risk by deciding the chances of anyone stumbling are too small to justify the \$7,500 expense. In this example, the property manager noted that no one has stumbled on the step for 20 years, then decided the cost of installing the railing exceeds the benefit of eliminating a small risk.



# UNIT 20

## Land-Use Controls and Real Estate Investment

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Explain the concept of police power and the provisions under which it protects the public's health, safety, and welfare.
- › Explain zoning ordinances, permits, building codes, and property use.
- › Describe the issues and regulations involved in subdivisions.
- › Explain nongovernmental (private) land-use restrictions: covenants, conditions, and restrictions (CC&Rs).
- › Identify the advantages and disadvantages of investing in real estate.

### KEY POINTS—UNIT 20

- The purpose of land-use controls is to promote efficient use of limited land resources.
- Zoning laws are also meant to protect the health and safety of the community's inhabitants. Buffer zones are used to separate areas with incompatible uses.
- Building codes set minimum standards for construction materials, plumbing and electrical components, and the structural integrity of a building. A building permit must be granted before construction can begin. A certificate of occupancy will be issued once the building is complete, and a final inspection verifies that the builder has complied with the codes.
- Zoning ordinances, which are set at a local level, may be amended. A zoning amendment must be justified by the needs of the community.
- A nonconforming use is a pre-existing use that was already legally in place when a new zoning ordinance came into effect. Although nonconforming uses are generally allowed to remain, they may be subject to certain restrictions. A nonconforming use usually cannot be rebuilt if it is destroyed.

- A variance provides permission to build a structure or use property in a way that would not otherwise be allowed. Variances are usually granted when strict compliance with the zoning ordinance would cause undue hardship to the property owner.
- A zoning authority can issue conditional use permits (special use permits) for uses that would ordinarily not be allowed in a zone. Permits are granted subject to conditions that limit the adverse effects of the use on the neighborhood.
- Buyers should call the local zoning department to verify that the use they anticipate for the property is allowed.
- The advantages of investing in real estate include a typically high rate of return; greater control over the investment than for other options; property appreciation over time that leads to equity buildup; leveraging of funds to provide greater purchasing power; and the tax benefits of depreciation, deductions, the use of a property exchange to postpone taxation, and treatment of income from a property sale as capital gain.
- The disadvantages of real estate as an investment include its lack of liquidity (it generally takes a long time to convert real estate into cash) and that it requires active management to ensure it is being managed property.

## I. LAND-USE CONTROLS

### A. Overview

1. Land is controlled through public and private limitations, as well as direct ownership by federal, state, and local governments.
  - a. More than \_\_\_\_\_ of the land area in the United States is privately owned.
  - b. The federal government owns more than 29% of the land, more than a third of which is in Alaska.

### B. Government ownership

1. Government-owned land is used for
  - a. national parks and forests;
  - b. military bases;
  - c. government buildings; and
  - d. streets, highways, and bridges.
2. The government's source of its authority to create regulations to protect the public health, safety, and welfare is its \_\_\_\_\_.

### C. The comprehensive plan

1. Local governments, municipalities, and counties establish development goals in a \_\_\_\_\_.

2. The plan is drafted by a \_\_\_\_\_ and typically covers the following:
  - a. Land uses
  - b. Housing needs
  - c. Movement of people and goods
  - d. Community facilities and utilities
  - e. Energy conservation

**D. Land-use classifications (set by local zoning laws)**

1. Residential
2. Commercial
3. Industrial/manufacturing
4. Agricultural
5. Mixed
  - a. Note: A \_\_\_\_\_ is an area of land that separates two significantly different land-use zones. Parks and open spaces are often used as buffer zones.

## **II. ZONING**

**A. Zoning ordinances implement the comprehensive plans**

1. There are no nationwide and very few statewide \_\_\_\_\_.
2. Zoning is used to regulate the following:
  - a. Permitted uses of each parcel of land
  - b. Lot \_\_\_\_\_
  - c. Types of \_\_\_\_\_
  - d. Building \_\_\_\_\_
  - e. Setbacks
  - f. Density
  - g. Protection of natural resources

**B. Zoning classifications**

1. Bulk zoning is used to control \_\_\_\_\_ and avoid overcrowding.
2. Aesthetic zoning is used to specify types of \_\_\_\_\_ for new buildings.
3. Incentive zoning ensures that certain uses are incorporated into \_\_\_\_\_.

**C. Zoning permits**

1. A building \_\_\_\_\_ must be issued before beginning any development.
2. A \_\_\_\_\_ use that existed before land was zoned may be allowed to remain.
3. A zoning \_\_\_\_\_ will consider an appeal about a zoning regulation.
  - a. A special property use may be allowed by issuance of a \_\_\_\_\_ permit.
  - b. A \_\_\_\_\_ will provide relief if a zoning regulation deprives an owner of the reasonable use of the property.

**III. BUILDING CODES AND CERTIFICATES OF OCCUPANCY****A. Permits**

1. New construction and most renovations require a \_\_\_\_\_.
  - a. Building permits are used to ensure that property owners are in compliance with \_\_\_\_\_.
    - i. State codes set minimum construction and safety requirements.
    - ii. Local codes may be more restrictive than state codes.
    - iii. If there is a difference between national, state, or local building codes, the most stringent is used.
  - b. A proposed building must first comply with zoning, or the property owner will have to seek a zoning change.
2. Building codes are primarily concerned with the structural integrity and \_\_\_\_\_.
  - a. Codes determine the types of construction materials that can be used.
  - b. Separate codes for plumbing, electrical, fire, and so on
3. A \_\_\_\_\_ (CO) is obtained after all the requirements of the building permit are fulfilled.



#### IV. SUBDIVISION

##### A. Subdivider and developer

1. The person who buys undeveloped acreage and divides it into smaller lots is the \_\_\_\_\_.
2. The person who improves the land by constructing homes or other buildings on individual lots is the \_\_\_\_\_.

##### B. Land development plan

1. The subdivider submits a \_\_\_\_\_ that must comply with the municipality's comprehensive or master plan.
2. Any proposed change to the comprehensive plan must undergo a lengthy approval process.

##### C. Subdivision plan

1. Individual lots are denoted by location and size on a \_\_\_\_\_.
2. The developer may be required to submit an environmental impact report.
3. Zoning authorities will consider \_\_\_\_\_ zoning standards.

#### V. PRIVATE LAND USE CONTROLS

##### A. Deed restrictions

1. Limitations on the use of property imposed by a past owner or the current owner by inclusion in the property \_\_\_\_\_

##### B. Restrictive covenants

1. Private rules set up by the developer that establish standards for all parcels in a subdivision are \_\_\_\_\_, or covenants, conditions, and restrictions (CC&Rs).

#### VI. REAL ESTATE INVESTMENT

##### A. Advantages

1. Investment in real estate typically produces \_\_\_\_\_ return over time.
2. More control than for other options
3. Appreciation
4. Equity buildup as principal and interest payments pay down \_\_\_\_\_ used to purchase the property
5. Tax benefits of depreciation deduction and 1031 \_\_\_\_\_

**B. Disadvantages**

1. Lack of liquidity, which refers to how quickly an asset may be converted into \_\_\_\_\_
2. Requires good property management
3. Presents a certain level of risk
  - a. Rents may \_\_\_\_\_ due to competition or the state of the economy.
  - b. Property values may \_\_\_\_\_.

## UNIT 20 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

1031 exchange	conditional use	tax benefits
agent's	grandfathered	uncontrolled building
amendment	health and safety	variance
buffer zone	local level	zoning ordinances
buyer's	nonconforming use	
certificate of occupancy	police power	

1. Planning, zoning, building codes, building permits, inspections, and certificates of occupancy are examples of local and state governments controlling land use and exercising the right of \_\_\_\_\_.
2. Local municipalities enact and enforce \_\_\_\_\_ as part of their right to govern land use under police power.
3. Permission to vary from strict compliance with zoning requirements may be obtained in the form of a \_\_\_\_\_.
4. Local authorities passed a zoning \_\_\_\_\_, which changed a large area previously zoned agricultural to residential.
5. When a previously established use does not comply with the requirements of a new zoning ordinance, it may be allowed to continue as a \_\_\_\_\_.
6. Many real estate investors feel that \_\_\_\_\_ help offset real estate's lack of liquidity.
7. A \_\_\_\_\_ may be used to separate two incompatible zoning uses.
8. Zoning laws are established at the \_\_\_\_\_.
9. Before a new building can be inhabited, a \_\_\_\_\_ is required.
10. Licensees should inform buyers that it is the \_\_\_\_\_ responsibility to verify that zoning and building codes will meet the buyer's needs.
11. Several neighborhood groups voiced support for an organic grocery store, which obtained a \_\_\_\_\_ permit allowing it to operate under certain restrictions and conditions in an area zoned for office use.
12. Investors and business owners can use a \_\_\_\_\_ to defer payment of capital gains tax.

## UNIT 20 GLOSSARY REVIEW ANSWERS

1. police power
2. zoning ordinances
3. variance
4. amendment
5. nonconforming use
6. tax benefits
7. buffer zone
8. local level
9. certificate of occupancy
10. buyer's
11. conditional use
12. 1031 exchange

# UNIT 20 QUIZ

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1. A disadvantage of owning real estate is
  - A. it requires a loan to buy.
  - B. its lack of liquidity.
  - C. the cost to sell is high compared to the value.
  - D. it appreciates.
2. An area of land that separates two drastically different land-use zones is
  - A. a buffer zone.
  - B. a setback.
  - C. a nonconforming zone.
  - D. a variance.
3. The distance that a zoning ordinance requires between a property's boundaries and its improvements is
  - A. a buffer zone.
  - B. a range.
  - C. a frontage.
  - D. a setback.
4. *Nonconforming use* is a term used in reference to property that
  - A. extends over lot lines.
  - B. is in need of deferred maintenance.
  - C. doesn't comply with current zoning requirements but may have been grandfathered in.
  - D. hasn't been recorded.
5. A light industrial plant has been operating in compliance with its zoning classification. After a zoning change to single-family residential use, the owners of the industrial plant will MOST likely be
  - A. required to convert the building to condominiums or other residential use.
  - B. grandfathered and can continue the present use as long as that use is not enlarged or expanded.
  - C. allowed to build an addition to the plant.
  - D. given a one-time option to rebuild the plant if it is destroyed by natural causes.
6. A developer is asking to be allowed to put 10 manufactured houses on a property that is zoned residential. Which of the following codes will the developer have to follow?
  - A. Local city code, which requires that all residential homes have at least 10 feet of separation and be compliant with current building codes
  - B. County code, which requires 15 feet of separation, concrete foundations, and compliance with current building codes
  - C. State code, which requires distances of 5 feet and allows block foundations
  - D. Federal code, which requires compliance with local building codes
7. A municipality has authorized the improvement of a particular property in a manner that is NOT in strict compliance with the zoning ordinance. This is an example of
  - A. a nonconforming use.
  - B. an amendment.
  - C. a conditional use.
  - D. a variance.
8. The document that confirms a new building has met all the minimum building standards and is the final regulatory step in the process before offering new construction for sale is called
  - A. a building permit.
  - B. a certificate of zoning.
  - C. a building code.
  - D. a certificate of occupancy.
9. A buyer wants to use a residential property for a small business. Before closing, the buyer should
  - A. apply for a special use permit.
  - B. check the zoning to determine whether the use is allowed.
  - C. call an attorney to request a variance.
  - D. apply for a sales tax license.

# UNIT 20 BROKER-LEVEL QUESTIONS

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1. Who is responsible for verifying zoning, permits, floodplains, and other property issues once a property is under contract by a buyer?
  - A. The listing broker
  - B. The buyer
  - C. The buyer's broker
  - D. All brokers and the buyer
2. Real estate professionals would be responsible for all of the following EXCEPT
  - A. calling about the zoning to verify whether it will meet the buyer's needs.
  - B. recommending that a buyer have a property inspection.
  - C. disclosing all environmental issues that might impact the property even if they are located outside the property boundaries.
  - D. verifying any statement a seller or a buyer makes that appears to be false.
3. A broker representing a buyer shows a home that has been recently renovated. Regarding the new improvements, if the buyer writes an offer on the property, the broker should recommend
  - A. the buyer ask the seller for a full accounting of all the work done and the costs.
  - B. the buyer not worry about the renovation because sellers always pull permits to do this type of work.
  - C. nothing, because the property should be in perfect condition now that the work has been done.
  - D. the buyer call the building department to see what permits have been pulled.

# UNIT 20 QUIZ ANSWERS

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1. **B** The answer is lack of liquidity. The lack of liquidity is a disadvantage of owning real estate as an investment compared to something that can be sold quickly, such as stock.
2. **A** The answer is a buffer zone. When adjoining or nearby properties are zoned for drastically different uses, municipalities often create a buffer zone to separate them.
3. **D** The answer is a setback. Front, side, and rear setback requirements establish the minimum distance between property boundaries and the improvements located on the property.
4. **C** The answer is doesn't comply with current zoning requirements but may have been grandfathered in. When zoning in an area changes, a pre-existing use may be allowed to continue as a nonconforming use.
5. **B** The answer is grandfathered and can continue the present use as long as that use is not enlarged or expanded. When a previously established use does not comply with the requirements of a new zoning ordinance, it may be allowed to continue only if the established use is not enlarged or expanded. This is often called grandfathering. Also, the use may not be resumed after it has been discontinued.
6. **B** The answer is county code, which requires 15 feet of separation, concrete foundations, and compliance with current building codes. The strictest code is the one that must be followed, and the county has the strictest code.
7. **D** The answer is a variance. Permission to vary or deviate from a zoning restriction comes in the form of a variance. Typically, the type of variance in this case would be a conditional use or special use permit.

8. **D** The answer is a certificate of occupancy. A certificate of occupancy is the final step to show that a new building meets minimum building standards.
9. **B** The answer is check the zoning to determine whether the use is allowed. The buyer is expected to verify that the zoning of the property will meet the intended use.

## Broker-Level Questions

1. **B** The answer is the buyer. The buyer is obligated to verify all these issues as part of the due diligence process. It is the broker's and sales associate's responsibility to inform the buyer of this obligation.
2. **A** The answer is calling about the zoning to verify whether it will meet the buyer's needs. Real estate professionals should not call about the zoning for buyers, or the real estate professional would take on the liability for the information being correct. They should recommend that the buyer call about the zoning. Licensees must recommend that buyers have a property inspection, disclose all material facts, and verify any statements that appear to be false.
3. **D** The answer is the buyer call the building department to see which permits have been pulled. The broker should recommend that the buyer call the building department to determine whether the seller did the work with a permit. If the work was not permitted, the buyer could also be liable for the work if the buyer purchases the home.





# UNIT 21

## Environmental Issues and the Real Estate Transaction

### LEARNING OBJECTIVES

*When you have completed this unit, you will be able to accomplish the following.*

- › Identify the basic environmental hazards the real estate professional should be aware of for the protection of client interests, as well as the personal risk of liability for nondisclosure.
- › Describe groundwater, water table, and the provisions of the Safe Drinking Water Act.
- › Describe the issues involved with underground storage tanks, and the associated legal requirements facing the property owner.
- › Explain the regulation involved in the creation and operation of waste disposal sites and in the control of brownfields.
- › List the various federal laws that protect the public from uncontrolled hazardous waste, as well as the liability issues facing those who violate any of these laws.
- › Explain the responsibilities and duties of real estate professionals regarding environmental issues.

### KEY POINTS—UNIT 21

- Many important environmental issues are regulated by the Environmental Protection Agency (EPA).
- Real estate professionals should know enough to recognize signs of contamination and other issues, inform all parties of the situation, and recommend inspections and further investigation.
- Residential real estate agents should know the disclosures sellers are required to make in accordance with federal, state, and local environmental laws.
- Inhalation of asbestos fibers can cause respiratory disease. Asbestos is a mineral used in building materials before 1978. It is prevalent in wall insulation, pipe insulation, boiler and heat duct wrapping, siding, and floor and ceiling tiles. When friable and crumbly, asbestos fibers become airborne and easily inhaled. Asbestos may be totally abated (removed) or the friable areas may be encapsulated.

- Lead-based paint can cause lead poisoning when inhaled or ingested. The paint was used widely across the United States before 1978. Federal law requires sellers of housing built before January 1, 1978, to disclose the possible presence of lead-based paint to buyers, whether or not a licensee is involved in the transaction. When real estate agents are involved, they must make certain all parties are in compliance with lead-based paint disclosure requirements.
- Radon is a naturally occurring, odorless radioactive gas that is carcinogenic if inhaled in sufficient quantity over a long period of time. Radon moves from the ground to the atmosphere. Modern building codes requiring weather-tight construction can trap radon inside a home. Testing can reveal a measurable buildup of the gas. Radon mitigation systems ventilate the gas to the exterior of the structure.
- Carbon monoxide (CO) is a by-product of combustion. It is a deadly, invisible, and odorless gas that causes unconsciousness quickly followed by death when inhaled even for a short period. The presence of CO is easily detectable using CO detectors. While new construction and renovation typically require the installation of CO detectors, codes vary from state to state.
- Mold will grow anywhere there is excess humidity or moisture and an organic substrate. Not all molds are hazardous. If found in housing, mold can be a hazard and may require remediation. Remediation involves cleaning and providing a remedy for the excess moisture source. There is no federal disclosure law for mold. The current or former presence of mold is a material fact. States vary on specific disclosure requirements. Buyers suspecting the presence of mold in a building should make the sale contingent on a mold inspection.
- An environmental impact statement (EIS) studies the impact a proposed project will have on a given area. If an EIS is being prepared, it is a material fact and must be disclosed by sellers in the vicinity of the proposed project.
- The Comprehensive Environmental Response, Compensation, and Liability Act (the Superfund) followed by the Superfund Amendments and Reauthorization Act are two pieces of federal legislation making landowners responsible for the remediation of hazardous waste sites and other environmental hazards.
- Underground storage tanks (USTs), hazardous waste disposal sites, and brownfields must be disclosed and may make a property unsalable.

## I. HAZARDOUS SUBSTANCES

### A. Asbestos

1. Asbestos can cause respiratory disease.
2. Asbestos was used before 1978 in a variety of building materials, including pipe and wall insulation, flooring, ceiling tiles, and siding.
3. It is harmful if the fibers are \_\_\_\_\_ (broken and potentially airborne). Inhaling the microscopic fibers can cause a variety of respiratory issues.
4. If a building is being demolished or renovated, \_\_\_\_\_ (removal) should be done by a licensed professional before demolition.
5. \_\_\_\_\_ (sealing in place) is often \_\_\_\_\_ than removal because there is less of a risk of exposing the fibers.

**B. Lead-based paint and other lead hazards**

1. Elevated levels of lead can cause serious and potentially fatal neurological damage; children and pregnant women are most at risk.
2. Federal law requires \_\_\_\_\_ of housing built before \_\_\_\_\_, to make a disclosure of the possible presence of lead-based paint on the property to buyers, even if a real estate licensee is not involved in the transaction.
3. Agents must inform sellers of their obligation to perform the following:
  - a. Disclose the location of any known lead-based paint
  - b. Provide a copy of any lead-based paint report on the home
  - c. Provide a copy of the EPA pamphlet on lead poisoning
  - d. Offer buyers a 10-day opportunity to have the home tested
    - i. Buyers may \_\_\_\_\_.
    - ii. If the inspection is not waived, buyers may terminate the contract during the 10-day inspection period.
  - e. Sellers are not required to perform a \_\_\_\_\_.
4. Licensees are responsible for ensuring the purchase contract includes acknowledgments from the buyers, the sellers, and all real estate professionals.
  - a. Real estate professionals must sign the lead-based paint disclosure and are responsible for making sure all parties are \_\_\_\_\_.
5. Property managers and landlords must give a similar disclosure and EPA pamphlet to renters if the property was built before 1978.
  - a. The renter does not have to be given the 10-day opportunity to test nor must lead-based paint be removed.
6. The Renovation, Repair, and Painting (RRP) program of 2010 covers construction firms, trades, and individuals performing any property renovation or repair that disturbs lead-based paint.
  - a. Must be certified in containment and cleanup of lead dust and debris
  - b. Must provide owners with the *Renovate Right* brochure before starting work
  - c. Property owners working on their personal property are exempt, but must be in compliance if working on their rental property.
  - d. Considered a material fact if the renovation was completed in violation of this rule

**C. Radon**

1. A naturally occurring colorless, odorless, and tasteless \_\_\_\_\_
2. Moves from the ground into the atmosphere
3. Creates a hazard if it is trapped in a building—can cause lung cancer
4. Impossible to detect without testing
  - a. Test kits are available and easy to use.
  - b. A radon professional can test for the presence of radon and recommend a mitigation plan to lower the level of radon in the building.
5. Radon is \_\_\_\_\_ by adding a ventilation system allowing the gas to escape to the atmosphere.

**D. Formaldehyde**

1. Formaldehyde is a colorless chemical with a \_\_\_\_\_.
2. It was widely used in the manufacture of building materials and many household products because of its preservative characteristics.
3. Formaldehyde is a volatile organic compound (VOC) and an indoor air pollutant that can be measured.
4. Formaldehyde is a probable human \_\_\_\_\_.
5. Urea-formaldehyde foam insulation (UFFI) was banned, but its use is again allowed.

**E. Carbon monoxide (CO)**

1. Carbon monoxide is a deadly odorless gas that is the by-product of combustion.
2. If combustion appliances, furnaces, and wood stoves are working properly and have proper ventilation, CO is not an issue.
3. Improper ventilation or equipment malfunction can cause a buildup of CO gas, which causes unconsciousness and, in short order, death.
4. Carbon monoxide is easily detected with a CO monitor/detector.
  - a. Many states require CO detectors.
  - b. Home inspectors should test for CO buildup and know the requirements for detectors.

**F. Polychlorinated biphenyls (PCBs)**

1. PCBs included more than 200 chemical compounds that are not naturally occurring. They are flame resistant and have been used in electrical equipment.
2. Commercial use of PCBs was banned in 1979, but they remain in the environment because of the difficulty of \_\_\_\_\_.

**G. Chlorofluorocarbons (CFCs)**

1. CFCs are nontoxic, nonflammable chemicals used as \_\_\_\_\_.
2. Older appliances, such as refrigerators and air conditioners, may leak CFCs and should be properly \_\_\_\_\_ of to prevent further leakage.

**H. Mold**

1. Not all molds are hazardous. Mold can grow anywhere there is oxygen, moisture, and an organic food source.
2. If found in housing, toxic mold can be a hazard and may require remediation.
3. \_\_\_\_\_ involves cleaning the affected area and eliminating the cause of the contamination, as per EPA and state regulations.
4. There is no federal disclosure law for mold. Some states have disclosure requirements.
5. Buyers may have a mold inspection.
6. Sellers must disclose if there was or is a mold issue.
7. Real estate professionals should be aware of indications of mold, such as a musty smell, water damage, high humidity, or water leaks.
8. Mold may not be covered by the homeowners insurance policy.

**II. GROUNDWATER PROTECTION****A. Overview**

1. Groundwater exists under the earth's surface in geological formations and forms the \_\_\_\_\_, the natural level at which the ground is saturated.
2. Groundwater can be contaminated by a variety of sources, including runoff from \_\_\_\_\_, leaking underground storage tanks, septic systems, and other sources.
3. The contamination can flow a great distance from the source, making remediation time consuming and costly.

**B. The Safe Drinking Water Act (SDWA)**

1. The SDWA was passed to protect public health by regulating the nation's \_\_\_\_\_ drinking water supply.
2. Most property disclosure forms require sellers to identify the property's \_\_\_\_\_.
3. Sellers should identify the type and location of any \_\_\_\_\_ used on the property.

**C. Wetlands protection**

1. What is now called the Clean Water Act was first passed in 1948 with the goal of protecting and improving the quality of \_\_\_\_\_.
2. Wetlands can be habitats for fish and wildlife and can serve as water storage and drainage areas.

**III. UNDERGROUND STORAGE TANKS (USTs)****A. Location of USTs**

1. Commonly found on sites where
  - a. petroleum products are or were used;
  - b. auto repair shops are or were located; or
  - c. commercial and industrial establishments, from chemical plants to dry cleaners and food-processing plants.

**B. Legal requirements**

1. Resource Conservation and Recovery Act (RCRA) gives the EPA authority to develop a program for property management of USTs, as well as hazardous and nonhazardous \_\_\_\_\_.
2. Federal and state laws require landowners to register USTs and follow strict requirements for installation, maintenance, monitoring, and recordkeeping.
3. A tank is exempt from federal regulations if it holds less than \_\_\_\_\_.
4. A tank used for farm and residential purposes can hold as much as \_\_\_\_\_ of motor fuel.
5. Also exempt are
  - a. tanks that store heating oil burned on the premises;
  - b. tanks on or above the floor of underground areas; and
  - c. septic tanks and systems for collecting storm water and \_\_\_\_\_.

**IV. WASTE DISPOSAL SITES AND BROWNFIELDS****A. Waste disposal sites**

1. Waste disposal sites are also called \_\_\_\_\_.
  - a. The landfill begins as a natural or excavated hole in the ground.
  - b. The hole is lined with clay or a synthetic liner.
  - c. Waste is layered with \_\_\_\_\_ in the landfill.
  - d. Soil is placed on top of the landfill in the final step, known as \_\_\_\_\_.

**B. Brownfields**

1. Brownfields are defunct, derelict, or abandoned commercial or industrial sites that may contain \_\_\_\_\_.
2. The Small Business Liability Relief and Brownfields Revitalization Act (Brownfields Law) was signed into law in 2002.
3. It provides funds to
  - a. assess and clean up brownfields;
  - b. clarify liability protections, particularly for the innocent developer who neither caused nor contributed to the contamination; and
  - c. provide tax incentives to enhance state and tribal response programs.

**V. ENVIRONMENTAL LEGISLATION****A. Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)**

1. Established an initial \$1.6 billion fund, called the \_\_\_\_\_, to clean up uncontrolled hazardous waste sites and respond to spills
2. The Superfund Amendments and Reauthorization Act (SARA) created an \_\_\_\_\_ immunity status.

**VI. DEALING WITH ENVIRONMENTAL ISSUES****A. Discovery of environmental hazards**

1. Technical experts who can study property and gauge the level of environmental issues are called environmental auditors or \_\_\_\_\_.
2. Such professionals usually also offer guidance about how best to resolve conditions found.

**B. Environmental site assessments**

1. Due care over environmental issues can be demonstrated by ordering an environmental site assessment (ESA).
2. A federally funded project requires performance of an \_\_\_\_\_.

**C. Disclosure of environmental hazards**

1. Most state laws require disclosure of known \_\_\_\_\_ regarding residential property of one to four units.
2. Some states require real estate professionals to disclose patent \_\_\_\_\_, even if the seller failed to disclose them.

## UNIT 21 GLOSSARY REVIEW

(Some words may be used twice, and some words may not be used at all.)

abatement	environmental impact	mitigated
carbon monoxide (CO)	statement	radon
CO monitors	Environmental Protection	remediation
disclosed	Agency	stigmatized
encapsulate	friable	Superfund
	lead-based paint	waive

1. In many cases, it is better to \_\_\_\_\_ asbestos than to perform a(n) \_\_\_\_\_.
2. \_\_\_\_\_ is an odorless, colorless gas that, if found at a dangerous level, is often \_\_\_\_\_ by adding ventilation.
3. Many environmental laws are under the enforcement authority of the \_\_\_\_\_.
4. Known environmental hazards are material facts and must be \_\_\_\_\_ by sellers and real estate agents.
5. Asbestos is hazardous when in a \_\_\_\_\_ condition, because inhaling the fibers is a known cause of cancer.
6. Federal law requires sellers of housing built before January 1, 1978, to provide a(n) \_\_\_\_\_ disclosure to buyers.
7. Although lead-based paint disclosure laws allow buyers a 10-day period in which to have a home tested for lead, many buyers \_\_\_\_\_ the inspection opportunity.
8. A deadly, odorless gas that is the byproduct of combustion, \_\_\_\_\_ can be controlled by properly ventilating fireplaces, gas-fueled appliances, and furnaces.
9. Carbon monoxide can be easily detected by installing \_\_\_\_\_.
10. Toxic mold in a home may require \_\_\_\_\_, which involves cleaning the surfaces and finding a remedy for the cause of excess moisture and humidity.
11. If a project is federally funded, a(n) \_\_\_\_\_ must be prepared.
12. Federal money from the \_\_\_\_\_ may be used to clean up a hazardous waste site.



## UNIT 21 GLOSSARY REVIEW ANSWERS

1. encapsulate, abatement
2. Radon, mitigated
3. Environmental Protection Agency
4. disclosed
5. friable
6. lead-based paint
7. waive
8. carbon monoxide (CO)
9. CO monitors
10. remediation
11. environmental impact statement
12. Superfund

# UNIT 21 QUIZ

---

- Who bears the obligation to disclose lead-based paint in residential properties built before 1978?
  - The seller
  - The seller and listing broker
  - The seller and all brokers
  - The seller and lender
- A defunct, derelict, or abandoned commercial or industrial site that may contain toxic waste is called a
  - landfill.
  - UST.
  - wetland.
  - brownfield.
- Radon is
  - considered a stigma that must not be disclosed.
  - harmless to adults.
  - an odorless and colorless radioactive gas.
  - not considered an issue unless discovered.
- The obligation of real estate professionals in a transaction involving a home built before 1978, which therefore may contain lead-based paint, is to
  - give the buyer the disclosure.
  - ensure the seller inspects the property and removes all lead-based paint.
  - ensure all parties are in compliance with the law.
  - give the buyer an EPA booklet and have the buyer sign the disclosure.
- All of the following pairs match EXCEPT
  - mold and humidity.
  - asbestos and friable.
  - radon and radioactive.
  - CO and odoriferous.
- Toxic mold can be caused by excessive moisture and humidity. Cleaning the moldy surfaces and addressing the cause of excess moisture and humidity is called
  - abatement.
  - remediation.
  - detection.
  - encapsulation.
- Asbestos is contained in various building materials, and can become hazardous if the materials are
  - covered.
  - encapsulated.
  - intact.
  - friable.
- Asbestos can be covered, wrapped, or otherwise sealed in place through a fairly simple process called
  - encapsulation.
  - remediation.
  - abatement.
  - obfuscation.
- The natural level at which the ground is saturated is the
  - aquifer.
  - wetland.
  - water table.
  - well.
- The nontoxic, nonflammable chemicals used as refrigerants are
  - polychlorinated biphenyls.
  - chlorofluorocarbons.
  - urea-formaldehyde foam.
  - lead based.
- The federally mandated lead-based paint disclosure is required in the sale of all homes built before
  - January 1978.
  - June 2017.
  - July 2010.
  - the present day.
- The process of retrofitting existing homes with a ventilation system designed to exhaust radon to the atmosphere is called radon
  - humidification.
  - encapsulation.
  - hypothecation.
  - mitigation.

# UNIT 21 QUIZ ANSWERS

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1. **A** The answer is seller. The seller or the landlord is the only one obligated to complete the disclosure. The real estate broker's obligation is to ensure all parties are in compliance with the law.
2. **D** The answer is brownfield. Many such sites can be found throughout the United States.
3. **C** The answer is an odorless and colorless radioactive gas. Radon is a naturally occurring gas that can accumulate inside a well-built structure.
4. **C** The answer is ensure all parties are in compliance with the law. The obligation of real estate professionals regarding lead-based paint is to ensure all the parties are in compliance with the law.
5. **D** The answer is CO and odoriferous. CO is an odorless, colorless deadly gas.
6. **B** The answer is remediation. Remediation is the process of removing mold, cleaning the surfaces, and providing a remedy for the moisture issues.
7. **D** The answer is friable. Asbestos is most hazardous in a friable state, meaning the fibers are broken, have become airborne, and are inhaled.
8. **A** The answer is encapsulation. Friable asbestos can be encapsulated in a manner that prevents the asbestos fibers from being disturbed and becoming airborne.
9. **C** The answer is water table. The water table may be several hundred feet underground or near the surface.
10. **B** The answer is chlorofluorocarbons. Although they may be safe in some applications, release of chlorofluorocarbons into the atmosphere may result, eventually, in depletion of the ozone layer.
11. **A** The answer is January 1978. The use of lead additives in paint was banned as of January 1, 1978.
12. **D** The answer is mitigation. Radon buildup can be reduced by the installation of a relatively low-cost radon mitigation system that ventilates the gas to the atmosphere.



# APPENDIX: ANSWERS TO FILL-INS

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## Unit 1: Introduction to the Real Estate Business

### Page 6

POIT  
itemize  
\$250,000  
\$500,000  
two of the five

## Unit 2: Real Property and the Law

### Page 16

Surface  
Subsurface  
Air  
attached to the land  
being permanent  
house  
fence

### Page 17

flowing water (R = river)  
standing water (L = lake)  
prior appropriation  
third party  
deed

### Page 18

is not attached  
to the land  
included  
bill of sale  
attached to  
fixture  
appurtenance  
intent  
Built-in  
Freestanding  
written contract  
excluded

## Unit 3: Interests in Real Estate

### Page 29

fee simple absolute  
reverter  
remainderman  
homestead  
not the legal owner  
contact an attorney  
security  
privately  
legal purpose

### Page 30

right to use the land  
dominant  
servient  
crossing a neighbor's land  
in gross  
servient  
utility

### Page 31

terminate by nonuse  
personal privilege  
public control  
land use  
zoning  
developed

### Page 32

private land  
condemnation  
take property

## Unit 4: Forms of Real Estate Ownership

### Page 42

an individual  
heirs or devisees  
limited to their investment  
undivided interests  
fractional  
legal advice

### Page 43

right of survivorship  
through probate  
Overrides  
as joint tenants  
PITT  
married  
in trust  
living trust  
testamentary trust

### Page 44

beneficiary  
 general partnership  
 limited partnership  
 limited partners  
 charter  
 partnership  
 (units)  
 common elements  
 tenants in common  
 Limited common

### Page 45

member  
 a nonprofit  
 own and finance  
 shares of stock  
 No deed

### Page 46

resort properties

## Unit 5: Land Description

### Page 56

measures in feet, compass degrees  
 shape or boundaries

### Page 57

point of beginning (POB)  
 “starting at” or “commencing at”

### Page 58

range  
 tier  
 640 acres  
 43,560  
 640  
 5 acres  
 \$42,500

### Page 59

map  
 the plat is recorded  
 urban residential

### Page 60

create or confirm a legal  
 description  
 spot survey  
 datum  
 property boundaries  
 Benchmarks  
 encroachments  
 mile  
 640 acres  
 43,560 square feet

## Unit 6: Transfer of Title

### Page 68

or  
 ee  
 or  
 ee  
 or  
 ee  
 or  
 or  
 ee  
 o  
 o  
 e  
 e  
 alienation  
 deed  
 executed  
 grantee  
 deed  
 a written deed  
 guarantee or prove ownership

### Page 69

18 years of age, sane, and sober  
 grantor  
 grantee  
 acknowledgment  
 describe only the land  
 something of value  
 acceptance by grantee

### Page 70

most promises or covenants  
 grantee/buyer  
 seisin (pronounced *see-zen*)  
 quiet enjoyment  
 Warranty forever  
 grantor’s ownership  
 previous encumbrances  
 Quitclaim deed  
 grantor/seller  
 liability

### Page 71

transfer tax  
 notorious  
 possession  
 use

### Page 72

the will  
 devise  
 personal property  
 escheat  
 no will  
 Wills must go through probate

**Unit 7: Title Records****Page 82**

state laws  
 does not prove validity  
 constructive or legal notice  
 priority  
 to be valid  
 acknowledged  
 constructive

**Page 83**

actual  
 constructive/legal notice  
 chain of title  
 cloud on title

**Page 84**

historical summary  
 current and past  
 Lists objections

**Page 85**

current status  
 history

**Page 86**

not covered by  
 Standard exceptions  
 Special exceptions  
 owner's policy

**Unit 8: Real Estate Brokerage****Page 96**

the brokerage  
 owns  
 all contracts

**Page 97**

must withhold taxes  
 signed  
 own work hours  
 always negotiable  
 brokerage firm sets its own rates  
 outside  
 are not set by law

**Page 98**

markets  
 \$1 million  
 \$100 million  
 not competent

**Page 99**

document exchange  
 video conferencing  
 networking  
 license status  
 sponsoring broker's name  
 advertisement  
 misleading  
 Electronic Transactions  
 electronic signature  
 written record

**Page 100**

Signatures  
 signatures  
 three months  
 up to 18 months  
 junk emails  
 unsubscribe  
 privacy  
 personal information

**Unit 9: Real Estate Agency****Page 108**

court decisions  
 legislature  
 real estate commissions  
 represent the interests  
 fiduciary relationship  
 fiduciary  
 principal  
 fairness and honesty  
 without

**Page 109**

employs  
 express agreement  
 seller representation agreement  
 buyer representation agreement  
 implied  
 compensation  
 confidentiality  
 lawful  
 Loyalty  
 affect a transaction  
 commingling  
 state law  
 forever  
 universal  
 general  
 special  
 limited  
 special agent

## Page 110

every state  
customer  
disclosure and written consent  
designated agents  
nonagent  
ministerial acts  
nonagent  
incapacity  
the property  
all parties  
Breach  
law

## Page 111

care and skill  
all facts  
value or desirability  
negligent misrepresentation  
property disclosure  
Sellers  
current knowledge  
might change a decision  
hidden defect

## Unit 10: Client Representation Agreements

### Page 122

seller  
if the seller finds the buyer

### Page 123

procures  
seller  
commission  
illegal  
unilateral  
cooperating broker  
subagent  
buyer's  
state law  
printed  
online

## Page 124

comparative market analysis  
compared  
Names  
owners  
lease option  
legal description  
improvements  
Zoning  
property taxes  
amenities  
disclosures  
real estate professional  
property owner  
property owners  
brokerage firm  
property  
price  
responsibilities  
Broker's

## Page 125

personal property  
equipment  
closing and buyer's possession  
closing  
ownership  
encumbrances  
home warranty  
termination  
protection  
seller  
hold harmless  
fair housing  
Antitrust  
Signatures  
Date  
principal  
brokerage firm

## Page 126

Destruction

## Unit 11: Real Estate Contracts

### Page 134

intent  
oral or written  
written  
express written documents  
a promise  
performance  
Only one party  
executory  
executed

### Page 135

all essential elements  
duress, fraud, or misrepresentation  
competent parties  
18  
sane and sober  
by a court

### Page 136

offer and acceptance  
contract  
communication of acceptance  
terminates the original offer  
omit material facts  
puffing

### Page 137

Consideration  
earnest money  
law  
real estate professionals  
executory  
sell  
buy



**Page 138**

contingency clauses  
 earnest money is returned  
 set price for a set time  
 land contract  
 equitable title  
 purchase money mortgage

**Page 139**

part of an offer  
 Modification  
 written and signed  
 contract rights  
 New contract replaces original  
 contract  
 void  
 earnest money  
 returned

**Page 140**

statute of limitations  
 Choose not to sue  
 completion of the contract  
 both  
 only to seller  
 money lost

**Unit 12: Real Estate Financing****Page 150**

low down payments  
 principal, interest, taxes, and  
 insurance  
 credit score  
 FICO score

**Page 151**

debt to income  
 loan-to-value ratio  
 evidence of the debt  
 defaults  
 entire balance  
 remaining balance of the loan  
 in arrears  
 in advance  
 usury  
 exempts

**Page 152**

transfer fee  
 1%  
 1%  
 simple  
 mortgagor  
 mortgagee

**Page 153**

beneficiary  
 Due-on-sale clause  
 sold

**Page 154**

Waste  
 take priority  
 original position

**Page 155**

sold to satisfy the debt  
 all liens  
 defaulted debt  
 the lender  
 friendly foreclosure

**Page 156**

missed payments  
 deficiency or personal

**Page 157**

Interest-only  
 balloon  
 economic index  
 retiree  
 rapid-payoff mortgage

**Page 158**

twice  
 aged 62 and older  
 single loan  
 one parcel

**Page 159**

lender  
 Broad-form  
 consumer insurance claims  
 all types of buildings

**Unit 13: Government Involvement in Real Estate Financing****Page 168**

deflationary  
 direct lenders  
 Mortgage brokers  
 licensed  
 register

**Page 169**

originated  
 secondary market  
 pools  
 standardized  
 conventional  
 agricultural  
 loan-to-value

### Page 170

Conforming  
jumbo loans  
80%  
lower down payment  
owner-occupied  
buyer and seller  
foreclosure  
owner-occupants

### Page 171

guarantees  
must occupy  
100%  
real and personal  
condominiums  
partial release clause  
future advances

### Page 172

improvements  
interim  
end loan  
take-out  
leasing  
lower  
permanent  
remains in place  
junior to the original lien  
\$100,000  
HELOC  
real estate  
25 times each year  
five times each year  
four installments

### Page 173

three-day right of rescission  
purchase or construction loans  
triggers full disclosure  
all loan costs  
all costs  
\$400  
\$4,000  
\$500,000  
misdemeanor

### Page 174

age  
marital status, age, and public  
assistance (MAP)  
low-income and moderate-income  
development and rehabilitation  
small farms  
federal review  
underwriting  
property type  
credit scores  
income, debt, and cash reserves

## Unit 14: Closing the Real Estate Transaction

### Page 182

final inspection  
survey  
easements and encroachments  
negotiated in the sales contract  
title evidence  
financing  
purchase agreement  
attorney  
closing  
certificate of occupancy  
fire and hazard insurance policy  
tax and insurance payments  
structure

### Page 183

cooperative housing corporation  
attorneys  
specified date of closing  
one- to four-family home,  
cooperative, or condominium  
federally related mortgage loan  
affiliated business arrangement  
escrow account

### Page 184

Loan Estimate  
Closing Disclosure  
*Your Home Loan Toolkit*  
referral fee  
three business days  
debit  
credit

### Page 185

an equal amount

### Page 186

seller's last day  
debit  
credit

## Unit 15: Real Estate Taxes and Other Liens

### Page 192

the payment of money  
encumbrances  
foreclose  
voluntary  
by law  
waiver  
satisfaction  
priority  
seller must clear

**Page 193**

payment of debt  
all property of the debtor  
foreclosable lien  
all other liens  
property value  
board of appeals

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Special assessments  
assessment roll  
security  
first mortgage lien  
junior liens  
perform labor  
notice of lien  
release of satisfaction of lien  
judgment  
writ of execution  
lis pendens  
writ of attachment

**Page 195**

probate  
a corporation

**Unit 16: Real Estate  
Appraisal**
**Page 202**

an opinion  
Appraisal Foundation  
licensing and certification  
closed  
currently

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not an appraisal  
federally related loans  
not required  
private mortgage insurance (PMI)  
data  
problem  
scope of work  
analyze  
opinion of value  
Reconcile  
final  
*Uniform Residential Appraisal  
Report*

**Page 204**

Demand  
desire  
Utility  
Scarcity  
Transferability  
probable price  
Actual sales price  
remains constant  
competitors

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highest value  
CMA or BPO  
increase  
increasing returns  
more  
diminishing returns  
valued separately  
assemblage  
Plottage  
regression  
progression  
all three approaches

**Page 206**

decreases  
increases  
residential property  
comparable properties

**Page 207**

special-purpose properties  
highest and best use  
reproduction cost  
replacement cost  
deterioration  
obsolescence  
obsolescence  
total  
capitalization rate

**Page 208**

potential gross income  
market rental rates  
effective gross income  
net operating income  
\$100,000  
\$24,000  
6%

**Page 210**

It is not an average

**Unit 17: Leases****Page 220**

lessor  
lessee  
reversionary right  
statute of frauds  
less-than-freehold  
estate for years  
estate from period to period  
termination  
pays rent monthly  
holdover tenancy

## Page 221

estate at will  
 estate at sufferance  
 capacity to contract  
 legal objective  
 meeting of the minds  
 valid consideration  
 quiet enjoyment  
 adequate notice  
 included  
 beginning and ending  
 security deposit  
 accessible

## Page 222

real or perceived disability  
 reasonable modifications  
 habitable condition  
 return the premises  
 type of property  
 damaged or destroyed  
 leasehold interest  
 less than  
 actual notice  
 mortgaged

## Page 223

renewal option  
 purchase option  
 right of first refusal  
 fixed rent  
 base rent plus expenses  
 net leases  
 gross income/sales  
 unimproved property  
 landlord's  
 long-term

## Page 224

royalty  
 buy the property  
 use the property  
 performed  
 cancel

condemnation  
 Eviction  
 Constructive  
 terminated  
 tenant must move

## Unit 18: Fair Housing

### Page 230

separate but equal  
 defense industry  
 inherently unconstitutional  
 voting rights  
 dependent children  
 age 55 or older

### Page 231

for any reason or in any situation  
 All media  
 FSBO  
 Senior housing  
 80%  
 55

### Page 232

channeling  
 Blockbusting  
 panic selling  
 Redlining  
 open to the public  
 at their own expense  
 life activities

### Page 233

may not charge  
 two years  
 investigate

### Page 234

keeping all records

## Unit 19: Property Management

### Page 244

property owners  
 income  
 value of the investment  
 owners  
 associations  
 syndicates  
 seniors  
 management  
 property management  
 agency

### Page 245

property  
 termination  
 responsibilities  
 principal  
 general agent  
 Maintain the value  
 Generate income

### Page 246

loss  
 comparison  
 tenants  
 rents  
 good relations  
 employment procedures  
 public accommodation  
 same  
 income and debt

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Avoid  
Control  
Transfer  
Retain  
ACTR  
hazard  
personal property  
General  
bonds  
actual cash value  
replacement cost

**Unit 20: Land-Use Controls and Real Estate Investment****Page 254**

60%  
police power  
comprehensive plan

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planning commission  
buffer zone  
zoning ordinances  
sizes  
structures  
heights

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density  
architecture  
developments  
permit  
nonconforming  
hearing board  
conditional use  
variance  
building permit  
building codes  
safety of buildings  
certificate of occupancy

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subdivider  
developer  
land development plan  
plat map  
density  
deed  
restrictive covenants  
above-average  
debt  
exchange

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cash  
decrease  
decrease

**Unit 21: Environmental Issues and the Real Estate Transaction****Page 266**

friable  
abatement  
Encapsulation  
a better choice

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sellers  
January 1, 1978  
waive the inspection  
lead inspection or pay for removal  
in compliance

**Page 268**

radioactive gas  
mitigated  
strong odor  
carcinogen  
destroying them

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refrigerants  
disposed  
Remediation  
water table  
waste disposal sites  
public  
water source  
septic system

**Page 270**

wetlands  
solid waste  
110 gallons  
1,100 gallons  
wastewater  
landfills  
topsoil  
capping

**Page 271**

toxic waste  
Superfund  
innocent landowner  
environmental assessors  
environmental impact statement  
(EIS)  
material facts  
property defects

# Notes

# Notes

# Notes



# Notes

# Notes

# Notes

# Notes